REVIEW OF THE EFFECTS OF DISASTER CONDITIONS ON WHEAT, SOYBEANS, AND FEED GRAINS PRODUCTION

HEARINGS

BEFORE THE

SUBCOMMITTEE ON
WHEAT, SOYBEANS, AND FEED GRAINS

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

MARCH 23 AND APRIL 6, 1989
MAY 19, 1989, AMARILLO, TX, AND
MAY 20, 1989, GREAT BEND, KS

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[2] Elected to subcommittee, May 11, 1989.

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REVIEW OF THE EFFECTS OF DISASTER CONDITIONS ON WHEAT, SOYBEANS, AND FEED GRAINS PRODUCTION

THURSDAY, MARCH 23, 1989

House of Representatives,
Subcommittee on Wheat, Soybeans, and Feed Grains,
Committee on Agriculture,
Washington, DC.

The subcommittee met, pursuant to notice, at 9:35 a.m., in room 1302, Longworth House Office Building, Hon. Dan Glickman (chairman of the subcommittee) presiding.

Present: Representatives Johnson, Volkmer, Penny, Sarpalius, Jontz, Campbell, Dyson, Marlenee, Stangeland, Roberts, Emerson, Smith, Schuette, and Grandy.

Also present: Representative E (Kika) de la Garza, chairman of the committee.

Staff present: Daniel E. Brinza, counsel; Vernie Hubert, associate counsel; Joe Muldoon, assistant counsel; John E. Hogan, minority counsel; Glenda L. Temple, clerk; Greg Frazier, James A. Davis, and Cliff Humphrey.

OPENING STATEMENT OF HON. DAN GLICKMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. Glickman. Why do we not go ahead and begin the hearing this morning. I do not think we are going to have any votes right at the beginning at 10, although we go in at 10. We will have some votes this morning, however, but my guess is they will not start until about 11, so we will do our best to accelerate this as much as possible.

I want to welcome members and our witnesses to this morning's hearing, and particularly welcome our representative from the Department of Agriculture, Mr. Milton Hertz, who runs the ASCS operation. I have a brief opening statement, I want to yield to the chairman of the full committee, Mr. de la Garza who is here, and then yield to other members for whatever comments they want to make.

The 1988 Disaster Assistance Act was unprecedented. It was the single largest, in terms of dollars, disaster act ever enacted by the Congress and it was written, passed, and signed into law with incredible speed. It was in that respect a fine example of the way which the Federal Government, when all parties cooperate, can respond effectively and quickly to pressing national needs. I am proud of the role of this committee under the leadership of Chairman de la Garza to see that that was done.

However, it was not a perfect bill. I am sure that this morning we will have the opportunity to discuss some areas of contention. That is part of this subcommittee's oversight function. It is also part of this subcommittee's oversight responsibility to ensure that the executive branch is implementing the programs we enact consistent with the intent of the Congress. I believe that we need to remain vigilant over all laws we enact and the way they are carried out to ensure that the executive branch stays mindful of the importance of congressional intent.

We will hear from witnesses representing a broad spectrum of agriculture, all of whom were affected by the drought and by the disaster bill. Let me make special note of the panel which will address the emergency feed programs. It was our determination and consultation with the chairman of the livestock subcommittee, who toiled tirelessly on writing that part of the bill, that since the feed programs do, after all, depend on the basic commodities over which this subcommittee has jurisdiction, to explore these issues, as well, today. That line of demarcation is sometimes a little hard to draw. Last summer, this subcommittee and Mr. Stenholm's worked very closely on these programs and I am pleased we can continue that relationship this morning.

I would mention just one other final thing as well. It is no secret that the central part of America is blowing away right now. There is a potential drought of incredible magnitude occurring on the High Plains area affecting Mr. Roberts and my area but also affecting all of the High Plains area. I will be especially interested today if Mr. Hertz can comment on a variety of issues affecting that, and whether that 1988 drought assistance package may be relevant to the current drought, whether producers who may have planted crops in 1988 will be covered by it, and other items under your jurisdiction which you think that wheat farmers and other producers out in the High Plains area may be able to get some assistance in a problem that is getting worse.

So I will stop my own comments now and I will yield to our distinguished chairman who was the prime person shepherding the drought bill through the Congress, Mr. de la Garza.

OPENING STATEMENT OF HON. E (KIKA) de la GARZA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

The CHAIRMAN. Thank you very much, Mr. Chairman. I thank you for the kind words, but since we work as a team, any credit should go to all the members and everyone that worked on this legislation. I think it is very timely that you hold this subcommittee hearing for the specific area of your jurisdiction, but really it impacts across the spectrum of agriculture.

Last week we had a briefing from the weather people at USDA and even though on the average they say it comes out to normal, you cannot tell that to the person who lives where it is dry. And there are several areas that lead me to say that the drought is not over yet, even though it is not on the front pages, it is not on the 6 o'clock news. There are many areas we have that still have concern, so I am glad that you will be dealing with these aspects.

I just want to mention a couple of items. One is that we are already hearing all the way from North Dakota down to my area of South Texas that we have not had any moisture, the dust is blowing, and if we put the seed in the ground, it is not going to germinate. It will just be an added expense, a wasted expense. But the regulation says that we have to plant and I would hope that the representative of the Department here would explore—I have sent word to the Secretary—but I would hope that you might explore this some here. What can we do to facilitate the continuation of the program and not have someone go and plant the seed and go to that expense, if it is not going to even germinate. It will just blow away or get eaten by birds or whatever. So I think that we should take a look at that.

Second, I might add something I have been shouting from the rooftops, but again it does not get on the front page, it does not get on the 6 o'clock news. I guess you know, those of you from out of town, what gets on the front page here, and I do not want to get involved in that, my wife will not allow it. But that is about the only thing that makes the front page or the 6 o'clock news. The other area of concern is that we need to continue shouting that people should and must, to the extent that it is available, buy crop insurance.

We have a commission studying crop insurance to see how we can make it better, so we can make it compatible with the needs of the producers and an economically viable system. We have that commission looking at it, but in the meantime, since the drought is not over, farmers should utilize every soil moisture conservation practice. They should buy varieties or hybrids that are resistant to arid conditions and will take less moisture, and they should buy crop insurance.

But that is not the purpose of your meeting, Mr. Chairman, but rather all of the areas concerning the drought, so I would hope that all of the members have their input here and witnesses that you might have. But specifically I would like the administration to address the issue: can we do something, do we have to change the law, or can it be done administratively, so some producer out there is not forced to plant when he knows that it is not going to work.

I thank you, Mr. Chairman.

Mr. Glickman. Thank you, Mr. Chairman. Mr. Stangeland.

OPENING STATEMENT OF HON. ARLAN STANGELAND, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MINNESOTA

Mr. Stangeland. Thank you, Mr. Chairman. First, I want to commend you for holding this hearing on the drought and relief bill and let me say that in spite of what the chairman says, we all take credit for that drought and relief bill, we could not have done it without his kind of very solid leadership, and willingness to work with the administration at a time that we were trying to put together legislation that would assist in the drought. And I frankly think that, and I hold it up to my constituents, as a Congress working in its finest hour, to write a drought relief bill almost into the heart of a campaign with no political upmanship, no partisanship was just a tribute, and the leadership of this committee to face up to issues.

You know it is interesting, I have had very very few complaints on the actions that we took with the drought relief bill and from those who complained, I do not think there was any way in the world that we could have satisfied them. But I have had complaints on how it has been administered, not so much the administration from out here, but more the administration on the State level, and I am going to get into that, but I commend you for that hearing and salute the chairman and salute the whole committee for what we were able to accomplish under some very very difficult circumstances.

We look forward to hearing from the witnesses.

Mr. **Glickman**. Thank you, Mr. Stangeland. Mr. Volkmer.

Mr. **Volkmer**. I just want to join and welcome the witnesses also, and I appreciate the chairman holding this hearing.

Mr. **Glickman**. Thank you. Mr. Roberts.

Mr. **Roberts**. Yes, thank you, Mr. Chairman, I wish to beg the indulgence of my colleagues, I do have a statement, and I want to thank my colleague, my friend from Kansas, and also Mr. Marlenee from Montana for calling this hearing. And I want to ask permission now, Mr. Chairman, to enter for the record statements that are very relative to our hearing on behalf of Senator Dole and Senator Kassebaum of Kansas.

[The prepared statement of Senator Dole and Senator Kassebaum follows:]

Bob Dole
Nancy Landon Kassebaum

STATEMENT BY SENATOR BOB DOLE
AND SENATOR NANCY KASSEBAUM

MR. CHAIRMAN, WE APPRECIATE THE OPPORTUNITY TO SUBMIT A STATEMENT AT TODAY'S HEARING ON THE IMPLEMENTATION OF THE 1988 DISASTER ASSISTANCE ACT.

THIS APPEARS TO BE A VERY TIMELY HEARING FOR US IN WINTER WHEAT COUNTRY, ESPECIALLY IN KANSAS. ALTHOUGH WE WERE NOT HIT AS HARD IN OUR STATE LAST YEAR AS THE CORN BELT WAS, IT SEEMS THAT WHAT GOES AROUND COMES AROUND, AND MANY PRODUCERS IN KANSAS ARE FACING A REAL DROUGHT DILEMNA FOR THE 1989 CROP UNLESS THEY RECEIVE SIGNIFICANT MOISTURE WITHIN THE NEXT COUPLE OF WEEKS.

STILL TIME FOR THE 1989 CROP

WE ARE TOLD THAT IF WE DO GET TIMELY RAINS IN THE NEAR FUTURE WE COULD STILL HAVE A SIZEABLE WHEAT HARVEST. WE HOPE THAT IS THE CASE. OTHERWISE, FARMERS COULD FACE A SHARP CUT IN INCOME IF THE DRY WEATHER FORCES MARKET PRICES HIGHER, BECAUSE PRODUCERS WILL FACE LOWER DEFICIENCY PAYMENTS AND HAVE FEWER BUSHELS TO MARKET.

LETTER TO SECRETARY YEUTTER

YESTERDAY WE SENT A LETTER TO SECRETARY YEUTTER URGING THE DEPARTMENT TO PREPARE A LIST OF DROUGHT-RELIEF OPTIONS AND THE POTENTIAL BUDGETARY IMPACT OF THESE OPTIONS. IF PRODUCERS ARE PAID LOWER THAN ANTICIPATED DEFICIENCY PAYMENTS AND HAVE REDUCED YIELDS, IT WOULD SEEM THERE SHOULD BE A POSITIVE IMPACT ON THE BUDGET GENERATING SAVINGS FROM THE MOST RECENT BASELINE CALCULATIONS. PERHAPS THESE SAVINGS COULD BE USED IN A SIMILAR FASHION AS LAST YEAR WHEN WE USED SAVINGS FROM LOWER DEFICIENCY PAYMENTS TO PAY FOR THE DISASTER ASSISTANCE ACT. SO WE'VE SUGGESTED THAT USDA DETERMINE THE AMOUNT OF POSSIBLE SAVINGS THAT COULD BE APPLIED TOWARDS DISASTER PAYMENTS OR TO EXTENDING THE 1988 DISASTER ASSISTANCE ACT TO CROPS PLANTED DURING THE 1988 CALANDER YEAR.

WE HAVE ALSO URGED THE SECRETARY TO DECLARE HAYING AND GRAZING ON A YEAR-ROUND BASIS AND TO MAKE IT AVAILABLE ON A STATE-WIDE BASIS RATHER THAN PLACING AN ADDITIONAL RESPONSIBILITY ON EACH COUNTY. WE HAVE ASKED THE DEPARTMENT TO GIVE US THEIR ASSESSMENT OF THE PERCENTAGE OF WINTER WHEAT NOW COVERED BY CROP INSURANCE AND WE HOPE THAT PRODUCERS WILL CONSIDER CROP INSURANCE FOR SPRING-PLANTED CROPS SINCE THE DEADLINE RUNS THROUGH MID-APRIL.

CONCLUSION

WE'VE ATTACHED A COPY OF OUR LETTER TO SECRETARY YEUTTER AT THE END OF OUR STATEMENT AND WOULD AGAIN URGE THE DEPARTMENT TO PREPARE A LIST OF OPTIONS SHOULD OUR WORST FEARS REGARDING DROUGHT CONDITIONS IN KANSAS BE REALIZED. CERTAINLY, FARMERS WOULD APPRECIATE KNOWING THEIR OPTIONS AS SOON AS POSSIBLE. THANK YOU.

BOB DOLE
KANSAS
141 SENATE HART BUILDING
(202) 224-6521

COMMITTEES:
AGRICULTURE, NUTRITION, AND FORESTRY
FINANCE
RULES

United States Senate
WASHINGTON, DC 20510

March 22, 1989

Honorable Clayton Yeutter
Secretary
Department of Agriculture
14th and Independence Ave. SW
Room 200A
Washington D.C. 20250

Dear Clayton:

We are becoming increasingly concerned about the dry weather conditions in Kansas and its potential impact on the 1989 winter wheat crop. Although winter wheat is a hardy plant and there may still be a possibility of significant improvement if the crop receives adequate rainfall during the next few weeks, the 90-day weather outlook for March through May shows that most of Kansas has received only 25-50% of normal rainfall, at least one-half of the state is in a moderate-severe drought and above normal temperatures are expected to continue.

Three-quarters of the Kansas crop has been rated poor to very poor. Despite a significant increase in seeding last fall, early estimates indicate actual production may be far below last year's reduced level. The absence of any noticable rain in the near future combined with a drought-reduced harvest could impose a severe financial burden on many winter wheat producers who will be faced with lower deficiency payments and fewer bushels to sell.

We urge the Department to begin to immediately explore drought-relief options that could be made available to producers and the potential budgetary impact of these options. It would be helpful to have the Department's figures regarding possible budgetary savings resulting from lower deficiency payments and reduced yields that could be applied towards disaster payments or through extending the 1988 Disaster Assistance Act to crops that were planted in the 1988 calander year.

We would also urge immediate declaration of haying and grazing on a year-around basis to allow producers who own livestock or are short on pasture or feed to take advantage of haying and grazing opportunities during the five principle growing months. We also urge haying and grazing be designated on a state-wide basis, rather than a county by county basis.

We further urge ASCS to begin to immediately process "failed acre" applications with the goal of allowing producers enough time once failed acres are verified to plant oats and/or other crops.

It would also be useful for USDA to give us an assessment of the percentage of winter wheat acres covered by federal crop insurance. We look forward to working with you on these and other options should the current weather prospects continue and the winter wheat crop face further deterioration. We appreciate your timely response to these suggestions.

Sincerely,

NANCY KASSEBAUM
United States Senate

BOB DOLE
United States Senate

OPENING STATEMENT OF HON. PAT ROBERTS A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. ROBERTS. My first comments on this issue really relate to the implementation of the 1988 act and I know that we have some frustrations with the rules and the details of any legislation that is passed and that is expected. There is one area that I received more mail and phone calls and personal visits in regard to producers than any other, and it involves the double-crop benefit calculations, Milt, and the constant midstream changes relative to eligibility.

I have written the Department in regard to this issue. The response seems to imply in some cases that Kansas farmers requesting benefits on double-cropped acres are trying to cheat the system, and that inference bothers me more than just a little. Now the basic situation is simply many producers and particularly in central and north central Kansas requested the disaster assistance on double-crop soybeans, and they planted those soybeans after determining, right after wheat harvest, that there was adequate top and subsoil moisture.

After being informed they would qualify on these acres, the farmers were notified November 11, that they had to have two of a 5-year double-crop history. I understand that, and this decision was sent to State and county harvesters well after many ASCS personnel had begun processing the paperwork and issuing the checks. Then the ASCS office has started recalculating the benefits and then came the second hurdle.

The producers were notified that they had to have a two of 5-year history on that specific farm or field instead of their overall history of operation. And again, the ASCS personnel had to recalculate the benefits and that caused some further delay and some further frustrations. Then came the calls that ASCS was adding any double-crop production into calculations for eligible single-crop soybeans, even if the double-crop beans had been ruled ineligible for benefits. If that sounds like a lot of gabby gop, I can assure you it sounded like that out in farm country as well.

I fail to understand how the Department really determined these producers were raising double-crop beans solely for benefits if, as was brought to my attention in several cases, these acres outproduced the regular crop acre. Second, I failed to see the equity in telling farmers that the USDA will not consider their loss on double-crop acres, but will consider the double-crop production in determining benefits for single-crop soybeans. And the net result is continued delay and frustrating confusion, both for our local ASCS personnel and for the producer.

I urge the Secretary to review his policies regarding double-crop acres and to restore some fairness on this specific concern. I want to talk a little bit about wheat.

The CHAIRMAN. Will the gentleman yield at this point?

Mr. ROBERTS. Yes, I would be happy to yield.

The CHAIRMAN. Because I have another meeting I must go to. Let me just read you this memo; it sounds like science fiction. This gentleman is a grower in Kleberg County, Texas. He applied for and received disaster assistance on both his spring and fall crops of cucumbers. ASCS has now notified him and requested that he repay the fall cucumber crop disaster benefits and that he repay a portion of his spring crop disaster benefits because his production on the fall crop needs to be added to his production on his spring crop, thereby decreasing his benefits.

ASCS is applying the general rule that benefits cannot be paid on the same crop grown on the same field. They do not distinguish between different growing seasons. To further complicate matters, if he would have planted the cucumbers in a different field or if he would have planted a different fall crop, cantaloupes on the spring cucumber fields, they would still be eligible for benefits. I hope the Department can apply their scientific knowledge and get us out of a mess like this. Thank you.

Mr. Roberts. I thank the chairman. I'm not sure what it is you said, but I thank the chairman. It is the same thing, I think, in terms of the double-crop situation we have, Mr. Chairman.

The Chairman. You cannot grow cucumbers twice on the same field and get payments for both crops. But if you change fields then you get paid for the two crops. If it is a different season and different crop, you get benefits for the two crops. But if you plant soybeans and soybeans twice, then you only get paid for one.

Mr. Roberts. I think I better go to the wheat situation and the drought. The chairman has expressed some understandable concern that I share in a sense of real frustration on my part and is shared by Senator Kassebaum and Senator Dole. We are at the very critical stage, as you know, Milt, of emerging from dormancy out there, and the estimates are now that we are about 65 percent of normal yield and it is going down.

On Tuesday, March 14, much of the Winter Wheat Belt was blasted by a return to the Dust Bowl. I have the headlines here in regard to the Kansas papers. We are in real trouble. And what I have tried to do in the letter to the Secretary, as of last week, is outline several contingency plans that I felt were very very important. I know staff has talked to you and I talked to the Secretary. And it does not look like, in terms of the weather forecast, that things are getting any better. I will not go over, what the five contingency plans, I already said that in previous hearing, Mr. Chairman, but I must say that I am more than a little concerned in regard to the pace of the Bush administration in regard to getting people on board to key policy areas where we must be able to come up with some specific answers. I do not mean this at all as a reflection on the gentlemen who have done a splendid job on behalf of the USDA and our farmers and ranchers who are serving on the panel.

But I would tell my colleagues that people are crawling out of train wrecks faster than this outfit is getting people on board down there to at least be able to answer our questions. I understand from a breakfast situation we had yesterday at the Republican conference, that there is a new standard for appointees. I am all for that, but I am almost to the point to think that we have a new standard for service now, and we are going to appoint a bunch of celibate monks down there who can pass the FBI test, in terms of these positions. And we are blowing away out in our country, and I cannot get any damn answers. And if you can see, I guess, obviously from my statement, I am a little more concerned about this than usual. I would hope that during this hearing we could get some specific timetables. Because if we wait till April or May, it is simply going to be too late.

[The prepared statement of Mr. Roberts follows:]

The Honorable Pat Roberts
Wheat, Soybeans and Feed Grains Subcommittee
March 23, 1989

REVIEW OF 1988 DISASTER ACT IMPLEMENTATION; RELATED ISSUES

I want to thank my colleagues from Kansas and Montana for calling this hearing. I ask permission to enter for the record statements relative to our hearing on behalf of Senator Dole and Senator Kassebaum.

My first comments on this issue directly relate to implementation of the 1988 Act. While frustrations with the rules and details of any legislation are expected, there is one area I've received more mail, phone calls and personal visits from producers about more than any other. It involves double crop benefit calculations and the constant midstream changes relative to eligibility.

I've written the Department concerning this issue. The response seems to imply Kansas farmers requesting benefits on double cropped acres are trying to cheat the system. That inference bothers me more than a little.

The basic situation is simple. Many producers, particularly in Central and North Central Kansas, requested disaster assistance on double crop soybeans. They planted those soybeans after determining -- right after wheat harvest -- that there was adequate top and sub soil moisture.

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After being informed they would qualify on these acres, the farmers were notified November 11 that they had to have a two of five year double crop history. This decision was sent to State and County offices well after many ASCS personnel had begun processing the paperwork and issuing checks.

ASCS offices began recalculating the benefits. Then came hurdle number two. Producers were notified that they had to have a two of five year history on that specific farm or field, instead of their overall operational history. Again, ASCS personnel had to recalculate benefits causing further delays and frustrations.

Then came calls that ASCS was adding any double crop production into calculations for eligible single crop soybeans -- EVEN IF the double crop beans had been ruled ineligible for benefits.

I fail to understand how the Department determined these producers were raising double crop beans solely for benefits if, as was brought to my attention in several cases, these acres out produced the regular crop acres. Second, I fail to see the equity in telling farmers that USDA won't consider their loss on double crop acres, but will consider the double crop production in determining benefits for single crop soybeans.

The net result is continued delays and frustrating confusion for producers and local ASCS personnel. I urge the Secretary to review his policies regarding double crop acres and to restore some fairness on this specific concern.

Now, let's talk 1989 wheat.

The 1988 drought continues in the High Plains. Our winter wheat crop is at the critical stage of emerging from dormancy. However, the extreme lack of moisture in Kansas and other winter wheat states has pushed the 1989 crop right to the edge.

On Tuesday, March 14, much of the winter wheat belt was blasted by a return to the Dust Bowl. In Kansas, rolling dust clouds driven by high winds forced the closing of major highways. Many farmers reported spending the day trying to take steps to prevent further damage to their winter crops, despite mixed signals on what the chiseling would to them relative to the farm program.

The immediate weather outlook doesn't predict much hope for precipitation. Most of Western Kansas hasn't had any appreciable moisture since before the crop was seeded last fall. But the problem isn't limited to dryland crops.

Crop advisors report that irrigated wheat fields are in poor condition because of the mild winter. Much of the irrigated wheat in my district didn't go into dormancy, leaving it extremely vulnerable to the Arctic winds that followed on the heals of several days of 70 degree plus weather.

Simply put, Kansas winter wheat producers are in trouble. Last week, I sent the Secretary a four-point plan for addressing Mother Nature's impact on the winter wheat belt. Those steps are:

1) Implement emergency haying and grazing provisions to help the farmer/stockman cope with the impact on forages.
2) Expedite implementation of procedures for making failed acreage determinations, and release acres to permit planting of a cash crop. This is especially critical for farmers considering planting oats -- they need to be planted by mid April.
3) Rescind those ASCS directives that have caused administrative logjams in local offices so producers can settle the books on 1988.
4) Finally, if the 1988 Act doesn't cover all crop planted last year, the Secretary needs to use his general authority to provide assistance to producers in a timely fashion.

I want to emphasize timeliness. Winter wheat was planted last fall. We harvest early in this summer -- if there's something to harvest. We can't wait for a midsummer decision.

Mr. **Volkmer**. Would the gentleman yield?

Mr. **Roberts**. I would be delighted to yield.

Mr. **Volkmer**. It appears to this gentleman from Missouri that the gentleman from Kansas is a little upset.

Mr. **Roberts**. A tad, just a tad. And I apologize to my colleagues on the subcommittee for taking this much time, but chalk it up to the fact we are going through a very difficult time out on the High Plains and I hope we can have a good hearing on these contingency plans, and I thank the chairman.

Mr. **Glickman**. And I hope you will understand that there is some clarity in Mr. Roberts statement right there. Mr. Sarpalius.

OPENING STATEMENT OF HON. BILL SARPALIUS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

Mr. **Sarpalius**. One thing I would like to say is that in my district we produce, and I have about 37 counties, we produce a large amount of wheat. In an average year during our wheat season, we get about 4 inches of rain. This year we have had a little over 1 inch and the wheat producers are hurting very bad, and I am anxious to see if there is anything that can be offered to these producers in my district, and I look forward to hearing your testimony.

Mr. **Glickman**. Thank you very much. Mr. Emerson, do you have any comments?

Mr. **Emerson**. No comments.

Mr. **Glickman**. Mr. Jontz.

Mr. **Jontz**. I do not have an opening statement.

Mr. **Glickman**. Mr. Smith.

OPENING STATEMENT OF HON. ROBERT F. (BOB) SMITH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OREGON

Mr. **Smith**. Mr. Chairman, I think, obviously this is a timely discussion witnessing the problems we have had in Kansas already and other parts of the country. I just want to point out to the subcommittee what I think was a yeoman's job done in the drought relief package of last year which you recall was narrowed to those people who actually lost crops. And we had a good debate on the question of how far we should try to assist farmers in drought conditions.

As a result of narrowing that assistance to those people who raised crops, I think we targeted the problem and we assisted farmers and there is very little, as has been witnessed here, very little concern about that drought relief package. I think as a result of that we are able now to come logically to the Congress knowing that the Congress can depend upon this subcommittee for judgmental decisions on drought, and we can help Kansas and other States which obviously have drought problems, and we can do it conscientiously, and we can pass legislation if necessary.

So I think that good work of last year prepared the way for this subcommittee to address the problems of drought in this country which will be acceptable to everybody. And I compliment you and our chairman and the people on this subcommittee who addressed this issue logically last year, and I am ready to act to help farmers in Kansas or any other place, but we have the basis laid for action. Thank you.

Mr. **Glickman**. I would point out, it was you, Mr. Smith, that was very much responsible for that bill. I remember looking at your face across the crowded room as you were an active participant in that. Mr. Campbell.

Mr. **Campbell**. No comment.

Mr. **Glickman**. Mr. Grandy.

OPENING STATEMENT OF HON. FRED GRANDY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF IOWA

Mr. **Grandy**. Thank you, Mr. Chairman. I want to associate myself with remarks to the gentleman from Oregon and merely say that, particularly to Mr. Hertz and Mr. Von Garlem from the Department here, that the drought assistance package is receiving uniformly high marks out in my area and that includes at the local ASCS level. However, I have, through constituents and although Mr. Gingerich of Iowa, Mr. Don Gingerich who is representing the National Pork Producers Council who will be testifying today, is not my constituent, he has provided some valuable counsel on the discrepancy between the delivery of crop assistance and feed assistance. If there has been one area where perhaps there has been an imbalance of assistance and delivery, it has been there.

And I will have some questions, Mr. Chairman, which I may not be able to ask in person because I may be obliged to be on the floor for part of the panel's discussion this morning, I would ask to include those in the record and have the Department respond. But I do want to say I am very pleased, at least on behalf of my constituents, with the job that has been done so far. We happily are not looking at a job condition at this point. Although another 2 weeks I expect the letters on haying and grazing to start.

And merely say that I hope that we can reach some kind of a satisfactory determination on why feed assistance has lagged so far behind crop assistance under the otherwise successful drought assistance act. Thank you, Mr. Chairman.

Mr. **Roberts**. Would the gentleman yield?

Mr. **Grandy**. I would be pleased to yield to my friend from Kansas.

Mr. **Roberts**. I feel compelled to associate myself with your remarks and that of my friend and colleague from Oregon. In keeping with the recent election and Republican conference, I have a new motto. It says, no more Mr. Nice Guy, and you can understand my blood pressure on the problems we are going through. Nobody likes blowing dust at 70 miles an hour, and I want to make sure that everybody in the room understands that my personal statements in regard to my frustration do not apply to the gentlemen on the panel. You have worked long and hard for many years on many difficult problems. It is a tremendous task for you people who are understaffed, and probably underpaid for the long hours that you put in. And I really appreciate all the past courtesies and the attention you have given for these very, very complex problems. So while my blood pressure is considerable, it is certainly in no way directed in any criticism to the gentlemen on the panel. They have done an outstanding job.

Mr. GLICKMAN. Mr. Johnson, any opening comments?

OPENING STATEMENT OF HON. TIM JOHNSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF SOUTH DAKOTA

Mr. JOHNSON. Thank you, Mr. Chairman. I just want to commend you, Mr. Chairman, for holding this hearing on a critically important subject, and I commend the panel as well for the cooperation and work that they assisted all of us with this past year in putting together a drought relief bill. As has been alluded to, I think the drought bill was well received and was basically a very favorable step taken to relieve a lot of distress across rural America, particularly in my State of South Dakota. It was a great assist.

However, a number of problems and concerns do remain and hopefully we will learn from this past exercise. I do have a number of questions relating to feed assistance, as Mr. Grandy has mentioned, as well as the crop insurance aspect of the bill, payments being calculated against disaster payments and feed assistance is a cause of some concerns for many of my people. The irrigated and nonirrigated yields being combined. I have had some concern about honey producers being left out all together. I think it was very manageable to find a way to document losses there, and the entire question of loss appraisal remains a concern, as well.

So hopefully through this hearing we will affect this process and be able to use the wisdom gained here in the future. I may not be able to remain to personally ask the questions, so I will be submitting further questions in writing. Thank you, Mr. Chairman.

Mr. GLICKMAN. Thank you. Mr. Dyson, do you have any opening comments?

Mr. DYSON. No thanks.

Mr. GLICKMAN. Mr. Penny.

Mr. PENNY. No.

Mr. GLICKMAN. Mr. Hertz, it is a pleasure to have you here and you may proceed.

STATEMENT OF MILTON HERTZ, ADMINISTRATOR, AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY THOMAS A. VON GARLEM, ASSISTANT DEPUTY ADMINISTRATOR, STATE AND COUNTY OPERATIONS, AND JERRY NEWCOMB, EMERGENCY OPERATIONS AND LIVESTOCK PROGRAMS DIVISION

Mr. HERTZ. Thank you, Mr. Chairman. With your permission, I will submit my very short testimony that summarizes where we are in the administration of the program at this time, and proceed with your discussion.

[The prepared statement of Mr. Hertz appears at the conclusion of the hearing.]

Mr. GLICKMAN. Without objection. I think that is a good idea. I have noticed that you have talked a little bit about disaster payments, emergency feed assistance and the aflatoxin issue in your statement, and it will appear as part of the record and if members have questions on these points, we will either do it directly or through writing.

I would ask my colleagues indulgence. I have received a letter from Mr. Traxler from Michigan who is the second ranking member on the Ag Appropriations Subcommittee. He raises some questions which he would like to put in the record and would like to be asked, and, if possible, without objection, they will be in the record. I will get you that letter and I will ask you to respond to his request. It is about dry beans, something that is important to him as well.

Let me first ask you this. The question is often raised about the applicability of losses suffered by Winter wheat producers now under the 1988 drought assistance package, since the crop was planted in calendar year 1988. What is the Department's position on the applicability of the 1988 Disaster Assistance Act to Winter wheat producers who may be suffering losses as a result of the drought that has been occurring?

Mr. HERTZ. Mr. Chairman, when Congressman Roberts sent his letter he made reference to using the 1988 disaster program as it might apply to the fall seeding of a 1989 crop. In visiting with our General Counsel and our chief policy people, we feel that the legislation is crop-year specific and would apply only to losses suffered from 1988 production and could not be used to make payments on 1989 losses.

Mr. GLICKMAN. So that is the Department's formal position?

Mr. HERTZ. Yes.

Mr. GLICKMAN. And so, therefore, as far as you are concerned if we wanted relatively similar coverage for this year's crop, we would have to pass legislation?

Mr. HERTZ. Yes, we feel that the legislation had sort of a sunset as far as time with the 1988 crop.

Mr. GLICKMAN. Do you know if there are any folks in town who have taken a contrary view to yours on the intent of the legislation?

Mr. HERTZ. No, not at this point, sir.

Mr. GLICKMAN. How would the Department feel about legislation to provide wheat producers and others with disaster assistance like we did in 1988?

Mr. HERTZ. I think, and certainly I cannot speak for the Secretary at this point in time, but if we reflect on past history in support of disaster programs, if there is legislation that is needed to make payments to farmers because of losses, we will administer it.

Mr. GLICKMAN. I realize that you are not involved in the making of policy, but if you had the same conditions occurring this year as occurred last year in other parts of the country, as far as you are aware, has there been discussion in the Department about legislation that would confer comparable benefits in a comparable fashion?

Mr. HERTZ. No, I am not aware of any discussions that would suggest that we would recommend legislation.

Mr. GLICKMAN. I would just like to ask you with respect to the 1989 crop of Winter wheat, I am going to ask you four questions which I would like you to respond to in writing by April 3, if possible. We are going to have a hearing on April 6 on the Winter wheat crop estimate, and there we may focus more specifically on the issues of what we are going to do with that crop.

But the questions are: (1) what are USDA's projections for wheat program costs for the 1989 crop if weather conditions do not improve, and how much will that be below the OMB baseline. That is very significant for us in terms of budget; (2) what options is USDA exploring for drought relief which relates again to my first question I talked to you about; (3) will USDA approve year-round haying and grazing in Winter wheat areas on an expedited basis; and (4) will USDA make any expedited determination with respect to failed-acreage decisions to make sure farmers have options. That relates to some degree to Chairman de la Garza's question and Mr. Roberts question about the need to go out and expend dollars when it is absolutely no reason to do so.

We need those answers as soon as possible. We are leaving today and will not be back until the week of April 3 or 4. That is when our hearing is. I will get these to you in writing so that there is no misunderstanding. I do not know if it will be you or somebody else testifying on April 6; do you know?

Mr. HERTZ. We do not know at this point.

Mr. GLICKMAN. But these are very relevant questions for us to make a judgment because people are asking us these questions from the field. I am going to stop now. We do have a vote. I think we will start with Mr. Stangeland, then we will go to vote and then we will come back. Go ahead.

Mr. STANGELAND. I will be very very brief. I have only one complaint on the administration of the program, major complaint, and that is the question of potatoes. And it is a very sore spot in my district, let me tell you. You know initially they talked about being certified growers in North Dakota and it is within the North Dakota and Minnesota State ASCS', and I gather they are the ones that established the rates.

Using the same figures, North Dakota recognized certified growers and I believe offered them something in the range of $7.45 a hundredweight for the potatoes at day lost. The commercial grower got something like $4.25—I am in the range, I am not sure I am exact.

Minnesota—all growers got the $4.25. After we brought this to your attention, there was a correction made that foundation and registered growers in North Dakota would get the high figure but not all certified growers. But no change in Minnesota. Let me tell you there are almost percentagewise as many foundation of registered growers in Minnesota as a total percent of all of the growers, as there are in North Dakota. And it just seems to me that somehow you have to correct what those State ASCS committees have done in equity and fairness.

You know, as well as I know, that railroad over there is not a wall. It is a river and they travel back and forth and they know what each are getting and they are growing those potatoes in basically the same ground and same valley, and that is the big complaint I have and it is a real sore spot up there with a lot of the Minnesota growers.

Mr. HERTZ. Just let me make a quick comment, Congressman. In establishing the yields and the values of yields in nonprogram crops, we relied an awful lot on our State ASCS committees and our sister agency NASS in providing us with production and price data. It is true that in this particular case two different States looked at this data in a different way. But I should point out that although the price for the foundation potatoes in North Dakota stays at $7 and some cents a hundredweight, the Minnesota farmers are producing foundation potatoes, also are being paid at that high rate.

Mr. STANGELAND. Has that been changed just recently now?

Mr. HERTZ. I think that was put to bed about 1 month ago, Congressman.

Mr. STANGELAND. I ran into this toward the end of February at the Krugston Craft shows where growers came to me. They had the letter from you and one paragraph which was in error, and I think we corrected that with you that to your knowledge there were no foundation and registered growers. And that did not make them very happy. I do not know who advised you that there were no growers up there in that category, but there are many of them.

Mr. GLICKMAN. Why do we not stop now, we have about 6 minutes to go to vote. We will be right back.

[Recess taken.]

Mr. GLICKMAN. Mr. Stangeland, did you finish your question?

Mr. STANGELAND. Mr. Chairman, I had finished my questioning. I just want to add again what I said in my opening remarks that by and large the disaster bill has met with a great deal of favorable comment and acceptance in my district and the only really sore contention was the contention on potatoes.

On the question of blending irrigated crops with nonirrigated, we tried to work that out and it was not workable, and I have not heard any corn producer really complain to any great length because he had to have his irrigated corn blended with his nonirrigated, thereby bringing up the field and reducing his payment. So I just think, except for the potato situation, it has worked reasonably well.

Mr. HERTZ. I can assure you, Congressman, that we just checked and the folks in Minnesota have been informed that if they have foundation potatoes, they are paid the same as they are in North Dakota.

Mr. GLICKMAN. Mr. Volkmer.

Mr. VOLKMER. Thank you very much, Mr. Chairman. I have to, Mr. Hertz, join with the gentleman from Kansas in giving a little bit of urgency to looking at this year's crop as a possible disaster in certain areas also, and I have part of my district, as you may know, already looks like it is going to be a disaster unless something happens.

We have soil that is a little moist in about 4 to 6 inches and from then on it is just powdery dry and you can go as far as you want to go. It can go till it gets to rock and clay or something real bad, and we are not getting the rains and we have farms drying out. I want you to know that. I am one of those who is going to be interested in renewing this just in the event that it does happen. Then maybe make some changes.

I first wanted to join with others in commending you all, and especially our county ASCS officers and our State officers in Missouri for the work that they have done. I had an area where payments have been made. There are, it still looks like some things that perhaps need to be cleared up.

I was reading the prepared statement of a witness we are going to have later on, Mr. Gingerich from Iowa, the National Pork Producers Council. It disturbs me a little bit, page 5, on the feed assistance. I thought we had this worked out. In fact, I was told in my district it has been worked out. Because it started out that you were doing it wrong.

I was instrumental in writing this thing in your bill that you would only determine the feed on hand based on the suitability of that feed for that particular livestock because I have got producers in my district, they are very diversified. They have beef cows. They have pork. They have hogs. They raise a lot of their own grain. They also raise soybeans and usually raise some wheat for some cash crop in the summer.

In the past years, you all have said that if he has got a whole bunch of hay out there, and he has only got a few cows and he has only got a little bit of corn, that you have to put all the feed together to determine how much feed you need for both of the types of livestock. That was past history. Then in 1985 we rewrote that specifically, but yet you were still interpreting it the old way.

We started out last year, I was informed by some of the producer, especially in this one county, and we brought it to the attention of the State and on up, and I understood it was turned around. But I read in this report here, for example, for a pork producer—now I will have to ask Mr. Gingerich later when he gets up if this is still the case.

In Iowa, it says a pork producer with excess pasture in hay with 2,000 pigs and two 4-H cows denied eligibility for the Emergency Feed Program. What is the status of that now? Are we facing on suitability of the feed for the particular livestock or are we still allocating hay for hogs? Hogs just do not eat that hay.

Mr. **Newcomb**. At the present time, as you stated, if the producer has strictly hogs, we only look at the grain that is available for the hogs or the type of feed that they would consume. If they also have other livestock such as dairy cattle, we look at the entire feed that they have on the farm and count the entire amount, whether it is hay, corn, whatever, against the producer.

Mr. **Volkmer**. For all the livestock?

Mr. **Newcomb**. For all the livestock, yes.

Mr. **Volkmer**. That was changed in Shelby County, Missouri. I will tell you why. If you people cannot read, and you cannot listen, then I do know damn well, I think I am going to sue you. I am personally, because either you are plain stupid and I am getting upset just like the gentleman from Kansas is, because when we wrote that law, we specifically say that the feed has to be suitable for the livestock. And hay is not suitable for hogs, or do you think it is?

Mr. **Newcomb**. It is my understanding that most hog feeds do have alfalfa in them, sir.

Mr. **Volkmer**. Pardon?

Mr. **Newcomb**. Most feed ingredients or feed mixes do have some alfalfa in them—hog mix that is. Another point is we are not sure how we would go about determining how much of the corn would go for the cattle, how much would go for the hogs, and so forth.

Mr. VOLKMER. The corn can go for the hogs. I do not care about that. Put the corn on the hogs. It is crazy to put hay on hogs. We are going to have to be specific in this and say exactly what feed for you all to be able to interpret it. Exactly, I guess, we will have to write, Mr. Chairman, in the law that they are only to allocate hay to beef and dairy cattle. And they allocate other feed to hog. Now because you see what you are telling me is if I have got hogs, and only hogs, and I have got hay and corn, you allocate the corn to the hogs and not the hay; is that correct?

Mr. NEWCOMB. That is right.

Mr. VOLKMER. I could have tons of hay out there and I could only have 5 bushels of corn. And I got 2,000 hogs, so I get emergency feed assistance. But if I have one cow out here sitting on the side—one cow, then it all gets lumped together. And I do not get any emergency feed assistance. Do you not see anything a little bit wrong in that at all, just a little bit?

Mr. VON GARLEM. Mr. Volkmer, if I may?

Mr. VOLKMER. Yes.

Mr. VON GARLEM. One of the big criticisms of the Livestock Feed Assistance Program has been, it has been so complex, it is very difficult to administer and one of the complaints that we have had is that while we were doing a pretty good job with the disaster system payment, we are very slow on getting through all the livestock. We have tried very diligently to make the process as simple as we can.

We do not require that specific feed that we cost-share on or that we let be purchased be fed to eligible livestock. We have eligible livestock, ineligible livestock, and so in order to effectively administer the program exactly the way you are saying we really need to, then we are going to have to break out the application and have an application for hogs, an application for each class of livestock.

What we have done is said that if a producer has only one class, then we will limit the feed available and feed cost-share to that class of livestock. But if a producer has different classes of livestock on the farm, we make all of the losses eligible. We make all of the losses and the feed on hand accordingly. I mean, I understand what you are saying when you say he is predominantly a hog producer, but he has two cows.

Mr. VOLKMER. I really do not care if he has 200 cows.

Mr. VON GARLEM. But what you are saying is now we have to break it down. We have enough trouble and we have put farmers through a lot of abuse with all the questions we ask. If we have to do it by class and accept an application by class, we have now added another tremendous complexity to the program which we already are being criticized for being too complex.

Mr. MARLENEE. Mr. Chairman, may I ask unanimous consent that the gentleman be given 5 additional minutes.

Mr. VOLKMER. Thank you very much.

Mr. MARLENEE. Then I want a minute after that.

Mr. GLICKMAN. The gentleman is recognized for 5 additional minutes.

Mr. **Volkmer**. Are your offices still using this thing and this thing in making your calculations?

Mr. **Von Garlem**. In some cases, we have an assistance program out there on the computer to help them, but that is the bottom line. That is the backup.

Mr. **Volkmer**. And you just do not have the time to sit and figure because there is a formula that is used on the feed systems. And it is calculated based on a base of, I believe, milo; is that correct?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. And there is a basic amount of feed that you allocate, which I think is too small, but you still allocate, different for cattle than for hogs; is not that right?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. So you still have to make some calculations. Now I am just asking you to make one more, that is all it is. If I have hogs and I have cows, I have to calculate, according to yours. I put the cows and hogs together after I figure out how much. In other words, if I have 40 hogs and I get 2 pounds a day at that, that is 80 pounds?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. If I have 100 cows and I get 5 pounds a day, that is 580 pounds of feed?

Mr. **Von Garlem**. Of need.

Mr. **Volkmer**. Of need, that is correct. Now let us do it the other way. Then I have to figure out the feed on hand, and let us say I have so much corn and so much hay. I have to do each one of those separate; do I not?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. They are separate figures out here and they are added together; is that not right?

Mr. **Von Garlem**. Correct.

Mr. **Volkmer**. Now, I take the hogs and I take the corn and I figure out if that is enough. I do not figure the hay and I do not figure the cattle. That is one figure; is not that right?

Mr. **Von Garlem**. Yes.

Mr. **Volkmer**. Then I take the cattle or the dairy cows and I figure that against what is left of the corn, if any, and the hay. If there is nothing left of the corn, just the hay; is that correct?

Mr. **Von Garlem**. Yes.

Mr. **Volkmer**. How complex is that?

Mr. **Von Garlem**. Substantially, because now you have got to compute the loss, the percentage of loss, how much eligible loss you have, and we compute the loss based on the livestock on the farm. If you are going to separate them, now we have got to start saying, we are going to compute loss by class of livestock.

Mr. **Volkmer**. That is correct.

Mr. **Von Garlem**. So you have doubled up on that requirement.

Mr. **Volkmer**. That is one additional calculation.

Mr. **Von Garlem**. That is one on each side of the equation of loss and need.

Mr. **Volkmer**. All right, one and one—10 minutes, 15 minutes.

Mr. **Von Garlem**. One of the big criticisms that we have is that we have a form that is too complex. We are asking too many questions. One of your cohorts is chomping at the bit to get after us about eligible feed on hand. It is very complex and we were trying to keep it as simple as we can by saying, that if you only have one class, we do the computations on that class. If you have multiclasses, we add all of the needs and all of the losses together to determine how much.

Because the fact is even after we compute the benefits, you do not have to feed them to that. You can turn right around and feed them to ineligible livestock because we do not make that requirement either. We try to give the farmer the maximum flexibility on what he does to his farming operation based on his loss and his need, of course.

Mr. VOLKMER. So what we have right here in the Congress and what we say, you just ignore?

Mr. VON GARLEM. No, sir. We do compute it. If there is only one class, if you have more than one class, then we compute it for all classes.

Mr. VOLKMER. You do not use the suitability applicable to livestock if you have more than one class of livestock; that is what you are telling me?

Mr. VON GARLEM. No. We determine the suitability and the feed suitability for all classes of livestock on the farm.

Mr. VOLKMER. You are still ignoring it, as far as I am concerned. You are saying one thing. I am saying another.

Mr. VON GARLEM. Yes, sir.

Mr. VOLKMER. And therefore as far as I am concerned, I do not know, you may not have been here when we wrote this language and specifically when we put it in, that drought relief bill, when I put it in by way of amendment. Because I had heard that you all were still doing that.

Mr. VON GARLEM. We were up until then.

Mr. VOLKMER. You are still doing it from what you are telling me.

Mr. VON GARLEM. Well, only if there is more than one class of livestock on the farm.

Mr. VOLKMER. I know that. You are still doing it. And that causes all kinds of problems out there. It is not fair. I do not have many hog producers that feed their hay to their hogs. I really do not. But yet they cannot get feed assistance from what you are telling me. They cannot get feed assistance for their hogs, if they have hay on hand, if they have 1, 2, 10, or 12, whatever number.

Mr. VON GARLEM. Yes, sir.

Mr. VOLKMER. And that is if we have any hay left over, over the number that they need total, you just allocate it all together just like those hogs are a bunch of cows?

Mr. VON GARLEM. We total up the——

Mr. VOLKMER. That is the way you do it. You do it just like they are a bunch of cows, and they are not cows.

Mr. VON GARLEM. I understand. We are not treating them like they are a bunch of cows. We are treating them like a bunch of eligible livestock of all of the classes that are available.

Mr. VOLKMER. Generic. They are just generic out here. They are just livestock.

Mr. VON GARLEM. They are generic eligible livestock.

Mr. VOLKMER. Mr. Hertz, you have heard all of this, what do you have to say now?

Mr. HERTZ. Congressman, I think, the only comment I would make is that realistically when we look at a farmer, whether he has classes of livestock or classes of feed, whether one is applicable to the other, is that we have to look at the total production of that farm. And if that producer's management judgment said that I am going to raise all hay and no corn, should we not look at his eligibility because he really has not lost any production on the corn side and vice versa, if it be that he did not plant any hay.

Mr. VOLKMER. Wait a minute, if he is buying all this corn, he is not eligible for emergency disaster assistance anyway.

Mr. HERTZ. That is true.

Mr. VOLKMER. He is not going to be eligible for it anyway. I am not talking about that person. I am talking about the person that does raise that corn, but he also raises hay because he has cows and he has hogs both. I have a bunch of those in my district.

Mr. HERTZ. I understand what you are saying, sir.

Mr. VOLKMER. And undoubtedly there must be some in Iowa from what the testimony of one of our later witnesses is. There must be some someplace else and to me, to be honest with you, if I can get somebody to file suit against you, I am not kidding you, because I am just irritated just all the way up to here.

For somebody who back in 1985 wrote it and said here exactly in the record, we will get a copy of the record and have to send that to you, exactly what we meant and you are continuing to do what you are doing. To me that is just like telling a Member of Congress, go jump in the lake. We do not care what you say; we are going to do it our way. That is what I get from it. And it makes me just a little bit upset, as the gentleman from Kansas gets sometimes.

Mr. HERTZ. Well, Congressman, I will assure you we will go back and look at those records and see what was the intent at that point in time.

Mr. GLICKMAN. The other thing too—if the gentleman gives back the balance of his time—is that if we are in the position to write a 1989 Disaster Assistance Act, we may want to take another shot at this, Harold, if we write another disaster assistance bill.

I yield to our ranking minority member, Mr. Marlenee.

Mr. MARLENEE. I would associate myself with the remarks of the gentleman from Missouri, Mr. Volkmer. You may not have been here when we wrote the specific clauses, and I think you have in hand now some of those clauses, Mr. Volkmer.

Mr. VOLKMER. Would the gentleman yield?

Mr. MARLENEE. I would be happy to yield. However, let me say this. You may not have been there, but I hope that you can read what our intent was in the conference report. Because there are a number of places, Mr. Von Garlem, where you people have deviated wildly. Perhaps you cannot read, if you allow your bureaucrats or the bureaucrats that you are, down at the agency to interpret and try to convey to you, to communicate to you what we said.

It is very clear in our conference report, but by the time it goes through your machine down there, anything becomes extremely complicated. I would like to see the room where all of this stuff is generated. The Department of Agriculture is the laughing stock of the American producer because of the regulations and complexities of what you are trying to put upon them. The laughing stock of the community out there. Once more you are embarrassing this subcommittee and the full Agriculture Committee by those complexities. I feel badly that the American producer has to put up with this kind of regulation.

If you say you are trying to simplify, I would like to know how it would look if you tried to make it complicated. I yield to my colleague.

Mr. **Volkmer**. Mr. Von Garlem, Mr. Hertz, it says here, eligible producers or the producers of this subsection, a "qualifying livestock producer" is a livestock producer who has suffered a substantial loss in feed normally produced on the farm, for such produces livestock as a result of the livestock's emergency, and as a result does not have sufficient feed that has adequate nutritive value and is suitable for each of such producers, particular types of livestock.

Now that to me seems very clear. Now undoubtedly it is not for you. Now if we have to rewrite it, I will rewrite it, but I want you to know that the reason we wrote that, and that was in the 1985 farm bill also, which was a direct change from what we had before, because back in 1983 when we had a drought in my district, you all were doing that through my pork feed producer and you were not giving them any emergency feed or anything, and so we rewrote it with the intent that you would have to divide it. You have not done so to this day. I thank the gentleman from Montana.

Mr. **Marlenee**. Let me call to your attention the fact that we had specific language in the conference report that the Department would not count Federal crop insurance claims as part of the producers feed on hand and would not count crops produced and in storage that were never intended for feeding purposes. Yet your bureaucrats, your agency out there continues to roll over that and we deal with that continuously out in the district, out in the States.

That was not the intent of Congress. You are taking an action that we specifically put in a conference report. Do you intend to continue that kind of action?

Mr. **Hertz**. Congressman Marlenee, I should tell you that we have gone through the rulemaking process to change the requirement that Federal crop insurance be counted as feed on hand. That is in the process of being changed.

Mr. **Marlenee**. Second, you mean you intend to change the law? Clarify that for me?

Mr. **Hertz**. No, to change our regulations.

Mr. **Marlenee**. To what?

Mr. **Hertz**. To change our regulations.

Mr. **Marlenee**. I thought maybe you were sending a package up here for us to enact that would change our intent. I am glad you clarified that. Under section 301, the act allows producers of program crops to plant a portion of the committed acres to soybeans, sunflowers, or other oilseed crops in short supply.

At a colloquy, Mr. Chairman, Chairman of the full Agriculture Committee, Kika de la Garza, the gentleman from Texas, on the floor of the House passed the bill that specifically clarified that this was in fact the case, and yet the Department continues to disallow, for instance, safflower from being planted on those permitted acres because they are in short supply. And the plants are about to close in Culbertson, Montana, because we do not have the safflower or the oil base that they need in that plant.

Where do we get relief? How is it spelled? Tell me?

Mr. HERTZ. Congressman, our counsel advised us that safflower was not specifically listed as part of the sunflower, soybean package and therefore would not be treated in that way.

Mr. MARLENEE. Is it an oilseed crop?

Mr. HERTZ. It is an oilseed crop, but I think we could also look to another provision in the——

Mr. MARLENEE. I think you better get new counsel. A counsel that has the producers' interest at heart. That is what we were elected for. That is what you were appointed for to represent the producers of the United States of America in programs that would enhance agriculture and stimulate the economy of the United States of America. Please, I apologize for interrupting.

Mr. HERTZ. I just want to make a further comment, Congressman, that there is a provision that a producer can use 20 percent of his base to plant to another nonprogram crop, and safflower would fit into that category. I also am aware, Congressman, that the processing plant in Culbertson, Montana, that you are talking about has finally decided to pay a value for safflower. They are out getting contracted acres in southwestern North Dakota and eastern Montana, and at this point, I believe they have all the safflower they can possibly hope to process in the coming year.

Mr. MARLENEE. In the coming year, provided we do not have a drought and switching to drought, my counsel advises me we have heard from them out there this week and they still do not have enough safflower to keep them going. I enter that into the record, so that the record is clarified.

You state on page 2 of your testimony, as of February 28, 1989, 558,000 producers received disaster payments and emergency feed assistance amounting to over $2.7 billion. We hear a lot about the cost of these programs, about the cost of the disaster program. Could you provide this committee with some kind of an estimate on what they would have received had there not been a drought under normal programs, so that we can offset it against the $2.7 billion to obtain what the true cost of the disaster program would have been? Is there any way that you can do that?

Mr. HERTZ. Tom tells me, Congressman, that as the drought package is being put together that the $3.9 reflected the savings that were going to be accrued because of the drought in saved deficiency payments.

Mr. MARLENEE. In other words the deficiency payment dollar figure has been deducted from the $2.9 or $2.7 billion?

Mr. HERTZ. No; there really is not a relationship there. I was talking about the overall program and its cost as it related to the savings because of the higher commodity prices. And the $2.7 at this point in time is merely a number to indicate how much money we have paid out at this point in time in administering the program.

Mr. MARLENEE. What I would like to know is you may have paid that out in disaster payments, but would that have normally been paid out in deficiency payments to these producers who received disaster?

Mr. **Hertz**. We could go back, Congressman, and look at what our projections were a year ago in January when we projected like $1.50 deficiency on wheat and relate those on the claims on wheat. I am just using that as an example. We could come up with some numbers.

Mr. **Marlenee**. My time has expired, and I certainly appreciate your coming before the committee because there are tremendous problems out there with the administration of programs and complexity of programs, and believe me there are times, if I could find that suite of rooms where you generate these complexities down at the department, I would go down there and devastate it. And perhaps you have looked yourself, but appreciate your coming up. I want to make you aware of those complexities and of the complexities of the sign up and I apologize to my colleagues for going beyond my time.

Mr. **Glickman**. Thank you very much, Mr. Marlenee. I want to ask you one quick question before I go to Mr. Sarpalius, and that is on the question on haying and grazing on set-aside acres. What position is the Department taking to date on that and what are you recommending to State directors?

Mr. **Hertz**. As far as recommendations, we have procedures in place that has certain requirements that if drought is in progress, if there is a loss of growing crops, growing pastures that would trigger that. And that is basically up to the State committees and to the individual counties to make those requests, that they should be identified as a disaster area and eligible for haying and grazing.

Mr. **Glickman**. Do you not make then recommendations to State directors? Do you just wait for it to come from them?

Mr. **Hertz**. For the most part we wait till it comes from them.

Mr. **Glickman**. The county-by-county determination is sometimes a difficult one when you have got a growing drought situation. My hope is the State director in Kansas makes the decision as soon as possible. But you say the existing procedures are what are going to be applicable?

Mr. **Hertz**. Yes. They have continued to be there and there is a procedure provided for that at some point in time when they feel that they should trigger this, they start the mechanism there to not look at an entire State as an example being eligible for the emergencies on ACR. Why we do it on a county-by-county basis and once the claims have come in, I think we can use last year as an example, we had about a 24-hour turn-around once those requests came to our offices.

Mr. **Glickman**. I am going to recognize the gentleman from Texas. I would say I have been pretty lenient on time, but we are probably going to have a vote in another 20 to 25 minutes, so I would ask members to stay as much as they can within the 5-minute time period. The gentleman from Texas? You have no questions? Then the gentleman from Minnesota? Oh, you have asked your questions. The gentleman from Kansas?

Mr. **Roberts**. Yes. Thank you, Mr. Chairman. I think maybe judging from the hearing, I am going to recommend to the White House personnel team that all future applicants for USDA policy positions have the skin of a rhinoceros, and maybe the thicker the better. I would also like to ask, Mr. Chairman, if I could submit for the record, several questions on behalf of my colleague and friend from Iowa, Mr. Grandy, who is on the House floor with an added labor matter and to submit this for the record to the Department and hope they can respond in about 10 days.

Mr. GLICKMAN. Without objection. And if they relate to the questions of our hearing on April 6, make sure that they are answered at the same time as our other ones are answered.

Mr. ROBERTS. I would like to proceed with one question and I hope it is not too repetitive. In the ongoing monitoring of the situation out there, there would be considerable benefits of giving producers early options in allowing the planting of oats or other crops in regard to the failed acre designation. And it is my understanding that that decision or that deadline is April 1 in regard to wheat country; is that correct?

Mr. VON GARLEM. I was not aware that there was a hard date. The concern, before we declare it dead, we want to make sure it was dead and there are all variations on that theme, but I have heard anything from, it is completely gone to it has turned yellow, it has chances of survival. Basically what we were doing was trying to decide when it failed. And basically we have provisions in place to allow farmers to apply for failed acreage and I was not aware that there was any limitation, calendarwise, on the time that we would accept that application in all sincerity.

Mr. ROBERTS. In the midst of blowing away last week, we were told April 1. I will have to get that cleared up. And I understand that you have to monitor this situation very closely, but my point is that we are going to have lines long and deep at the local ASCS office and if we could proceed with that now.

It is only, what 7 to 10 days away in terms of April 1, but that procedure could be expedited, it seems to me, and I know there is going to be a tremendous load on your personnel out there to really get out in the field and to monitor that. I think the sooner we start that, the better off we are going to be. I can assure you there has been considerable damage, I know you are aware of.

But if the producer can go to some other crop and hope they will get some rain, I do not know what is going to grow if wheat does not grow. But at least if we are blessed with some rainfall that could provide some income help to alleviate the situation as we consider the emergency legislation here to provide whatever kind of disaster assistance may be forthcoming, plus the Federal crop kind of benefit. It would just help in terms of cash flow situation, as we go through a rough time.

So I will check again with our State ASCS folks and hopefully that April 1 threshold could be moved back, as of tomorrow or whatever. I have no further questions, Mr. Chairman.

Mr. GLICKMAN. Thank you very much. Mr. Jontz.

Mr. JONTZ. Thank you, Mr. Chairman. I do want to take a minute to relay my thanks in particular to the county ASCS office, Indiana, and my district that have worked very hard to implement this legislation. I really appreciate the work that a lot of your employees did and are doing. So thanks, very much.

Mr. GLICKMAN. Would the gentleman just yield on that point?

Mr. Jontz. Yes.

Mr. Glickman. I think it is worth mentioning that even though we criticize policy issues, your people do yeoman's work out there in the field. They have an incredible increase in the workload. They are required to make all sorts of on-the-spot decisions that require the wisdom of Solomon and while we do not always agree with the policy, I must commend you on your folks out there. They are really working hard and they are a credit to Government service.

Mr. Hertz. Mr. Chairman, if I just might say for one example. I had a call from a Congressman one day complaining about how long it was taking the payments to get out. This was in a county where of record we had approximately 300 producers that participated in our programs. Over 2,000 people walked in and asked for disaster payment. And I can promise you, if we have an office sized and we have it equipped and we have it staffed to serve a normal traffic of 300 producers and we get hit with 2,000, we not only have an accident waiting to happen, but we have a wreck.

I think there probably was three permanent full-time and then as many temporaries as they could stack in the room. But this particular office started scheduling. They worked overtime. They worked Saturdays and Sundays in order to get the job done. You are absolutely right, they are the MVP's of the agency.

Mr. Jontz. There is no question that your employees have done an outstanding job in implementing the legislation and we all do appreciate that. Mr. Hertz in your statement you note that as of February 28, 558,000 producers have received payments or assistance amounting to $2.7 billion. Can you supply us with some additional statistics perhaps, I would be interested in knowing how many applications are now pending and what you predict the total expenditure will be when all of the pending applications are dealt with?

Mr. Hertz. Yes, we can do that. I think right now we have projected that $2.7 billion represents approximately 70 percent, and if that be the case and the payments run in a similar amount, that $3.9 billion would certainly be a very close ball park figure.

Mr. Jontz. I appreciate that, and it would be helpful if that information could be forwarded as it becomes available. Do you have a breakdown of the distribution of disaster assistance by crop; is that something that you could also make available?

Mr. Hertz. We have broken it down by State now. I am not sure how detailed we have the breakdowns in total summary, but——

Mr. Von Garlem. Mr. Congressman, we will eventually have that data because we have at least set up our system to collect the data by crop this year, but there is so much lagging right now, the data really does not have much validity, but we will have that data available.

Mr. Jontz. Mr. Hertz, do you have any estimates in terms of how much was saved in spending on commodity programs as a result of the drought?

Mr. Hertz. I think the projections that were used when the disaster legislation was being prepared was that based on then calculations $3.9 billion would have been saved in outlays because of deficiency payments.

Mr. Von Garlem. We are not aware that those estimates have been updated. We will check and try to get it for the record, if they have been updated.

Mr. Jontz. I think it would be of interest to the committee and I am not sure what all these figures may eventually show, but I think that American agriculture, particularly as we look at the budget and we are asked to absorb additional budget cuts, deserves an accounting of how much was saved, how much was spent, who the money would have gone to had we not had the savings, and who the money went to under the disaster program.

I think it would be helpful to us to understand the total picture to a greater extent than we do and as expeditiously as you can provide that information and get some updates. I think it would be very helpful, particularly as decisions are made about the budget, I think that it is possible, that if we could show the fact that there was a savings to the Government, if disaster payments end up to totaling less than what the savings was.

Obviously, I think that is something that this committee needs to understand and all of us, in particular, of corn producing areas where, of course, a big chunk of the commodity program costs are, are aware that savings in terms of our programs have made it possible for the disaster payments.

I just wanted to ask for that information, as soon as it is available.

You also spent some time in your statement, Mr. Hertz, dealing with the problem of aflatoxin contamination. Let me ask you this question. If I am a producer and I have some corn stored at the present time, and I take that grain out of storage this summer or this fall to use it, and I find that there is appreciable aflatoxin image that has occurred, how could I at that point apply for disaster assistance, given that the deadline is March 31? Do you have some way of extending the date?

Mr. Hertz. Congressman, we have set March 31 as the final date for application, and May 15 as a date for the paperwork or the evidence, so to speak in this case of aflatoxin to substantiate or support the loss. That is where we are on it now.

Mr. Jontz. It seems to me that the producer is likely to have a correct picture of the damage only at the point when the grain comes out of storage and is used, and I wonder whether some flexibility might be instituted in the process, so that the producer who does not get his grain out of storage for the deadline, and then discovers the damage would have a chance to have a fair consideration of his application for damage. He suffered damage and it seems to me that the factor that we have to consider is that people might not know what damage they have until they get the grain out of storage. Am I mistaken about this?

Mr. Hertz. No. I think your observations are correct and the uniqueness of aflatoxin and being able to detect it, we suggested that farmers probe their bins and check them to see if it is present. We are informed that sometimes it is in tiny pockets and you cannot find it and probably will not know until it is taken out of that bin. We feel that we want to put a sunset on the 1988 disaster program and felt that, in fact, the legislation prescribed that March 31 would be the final date for application and then we added another 45 days for producers to bring in evidence to support their claims.

Mr. JONTZ. I am sure that you want people to take that deadline seriously, and I appreciate that. But perhaps I could just plant the thought in your mind that once that deadline has passed, if we do have some producers in that situation, I think it would only be fair to allow some extensions for those individual circumstances where the extent of the damage could not be determined or would not be easy to determine before the March 31 date.

I know my time has expired, but I would like to get one other brief question, if I might. There has been some controversy over disaster payments for preventive planting. As I understand the policy in Indiana it is determined on a county-by-county basis. Producers have a right to appeal to the State, the State has not overturned any county rulings.

Under usual procedures producers have a right to appeal decisions at the State level to Washington. This right of appeal is not available for a decision concerning preventive planting. Do you think that it would be a good idea, given the rather uneven interpretation of this policy at the local level to allow appeals to Washington on preventive planting?

Mr. VON GARLEM. If I may. Congressman, one of the concerns that we had with the disaster program since—and I listen in on a lot of appeals—but the bottom line on disaster and preventive planting really comes down to the determination that local county committee and possibly the State committee of the conditions that existed in that area at that place. And it has been my experience that trying to sit here in Washington does not help it. It just messes it up more. And that is why we tried to limit that to the State committee because essentially the data only gets softer as it comes to here and the reality of it is I have tried to never put myself in a position to know more about what is happening in that county than that county committee. And that was our concern.

Mr. JONTZ. I think my constituents would share your observation that sometimes things get more messed up in Washington. But the fact of the matter is that it is not just local circumstances that result in different decisions. In fact, there are different philosophies, and a producer could have a farm in two different counties and come up with two different results with the same situation. Because this question has been given to the county directors and county committees that is very broad and relates more to philosophy, than it does to the circumstances that are there. And I would think that a producer should have some guarantee of uniformity of due process.

I would ask you to reconsider your policy because, in fact, there are wide differences in terms in philosophy that do not have to do with what the actual facts of the matter are. And I think the producer could make a good case in some circumstances that that was the reason that he was denied benefits and not what the actual facts of the matter are.

So I would ask you, I do not know if there are a large number of those cases in our State, but I think there are a few and I would ask that you reconsider that policy. And I appreciate the patience of the chairman. I have over extended my time.

Mr. GLICKMAN. The gentleman from Indiana also had a key role in the drought assistance, but particularly with respect to those who suffered very significant losses, and I think his point is a good one. The gentleman from Oregon, Mr. Smith.

Mr. SMITH. Thank you, Mr. Chairman. Another policy issue, Mr. Hertz. Several of our livestock producers signed up under existing programs in the early spring of 1988. They were accepted by the county committee. They signed their agreement with the Department and they made their feed purchasing plans and marketing plans on that agreement. Fifteen days after the enactment of the 1988 drought bill, they were dropped from the program because of a change in the eligibility requirements of the 1988 program.

The legislation that was passed clearly expressed the desire of Congress to hold on to those participants, even though they had filed earlier and to make them part of the program and very quickly, I refer you to sections 604 and 605 of the act and I will read them quickly because it will make my point:

> Notwithstanding the proceeding provisions of this section, any State, county or area determined eligible due to drought or related conditions in 1988 for the Emergency Feed Program or Emergency Feed Assistance Program cannot be prior to the effective date of this title, shall continue to be eligible for such program, and may be eligible for other programs under the title, et cetera.

605:

> Any livestock producer located in a county or area in which benefits under the Emergency Feed Program or the Emergency Feed Assistance Program were made available due to drought or related conditions in 1988 prior to the effective date of this title who qualify for assistance under such preexisting programs, shall be eligible for assistance for such drought or related conditions as prescribed.

It is rather clear the intent was to take care of those people who had filed earlier then the enactment of the 1988 act. Now why did the administration drop many of those producers, all of them who had signed up early and in good faith, and then were eliminated from the program after the 1988 act was in place?

Mr. NEWCOMB. I am assuming that they were determined not to be eligible because they were not significantly engaged in grain or livestock or because of the $2.5 million limitation.

Mr. SMITH. I am sure those were the reasons.

Mr. NEWCOMB. In talking with our Office of General Counsel, they tell us that those two provisions supercede the language in sections 604 and 605 that you just read. So even though they were eligible prior to August 26, if they did not meet those two criteria on that date, they were no longer eligible for the program.

Mr. SMITH. As I understand it, the county committees have an opportunity to look at requirements of income and eligibility and they were screening people prior to the 1988 act; is that correct?

Mr. NEWCOMB. Not that I am aware of, sir.

Mr. SMITH. I am aware of those conditions. How many producers are in that category; do you know? How many producers were dropped as a result of this decision?

Mr. NEWCOMB. I really have no idea. We do not get such a report.

Mr. SMITH. Is there any alternative or wiggle room in the Department for some sort of negotiation on this issue, rather than a lawsuit?

Mr. Hertz. Congressman, we felt that the language was quite clear when they talked about gross income that would make certain producers ineligible.

Mr. Smith. That was after the fact though, you have to admit that. That was not the case prior to the 1988 act.

Mr. Hertz. That is true.

Mr. Smith. These people were accepted. The county committees accepted them. They signed up for the program. I am going to visit with you about this again, but it seems to me that the direction of the act was carefully drawn and you are either eligible or you are not. The verbiage in the act directed, so far as I can read it and I read it to you, that those people eligible prior to the program that had signed up and were accepted should be eligible after the program, despite the different qualifications in the 1988 act. That is a discussion point.

Mr. Hertz. We would be happy to visit with you on it, Congressman.

Mr. Smith. Then on another subject of the question of Federal crop insurance, let me ask you if the ASCS will retroactively provide assistance to livestock producers who were earlier denied benefits because they had crop insurance?

Mr. Hertz. Yes. We would go back and make them all.

Mr. Smith. Mr. Chairman, I have several other questions that I may submit in writing, and hopefully, we can have an answer by our April 6 meeting. I will not take up any more of your time.

Mr. Glickman. I would ask Mr. Hertz from the Department to answer Mr. Smith's questions again at the same time, if it is feasible. And also I have questions submitted by Congressman Stenholm, the chairman of the Livestock, Dairy, and Poultry Subcommittee, and some of these are very detailed specific questions in the operation of the program for hog and cattle producers. I appreciate your answering those as well.

I would now recognize, Mr. Dyson. By the way you have gotten these specific things. I think maybe what we ought to do in your answering the questions, the four questions that I asked you, you respond directly back to me. Mr. Traxler's, Mr. Grandy's, and Mr. Smith's answer to them. But all of the answers will be made a part of the hearing record at this point.

[The material follows:]

QUESTIONS FROM THE HEARING MARCH 23, 1989
SUBCOMMITTEE ON WHEAT, SOYBEANS, AND FEED GRAINS
COMMITTEE ON AGRICULTURE

Questions for the record from Chairman Glickman:

1. What are USDA's projections for wheat program costs for the 1989 crop if current weather conditions do not improve to at least normal and average?

Answer: The President's Budget presentation to Congress on February 9, 1989, estimated deficiency payments for the 1989 crop of wheat to be about $1 billion. The forecast was made as of late November, with a projected wheat farm price of $3.60 a bushel and expected yields slightly below trend. Estimates have not been updated since that time. However, based on conditions that have developed since late November, crop prospects, especially in Kansas, have deteriorated. As a result, our production prospects are likely somewhat lower and price expectations are higher. This would suggest program costs below $1 billion at this time.

2. How will those projections compare to the present OMB baseline for spending associated with the 1989 winter wheat crop?

Answer: With poor weather conditions for the winter wheat crop it appears that yields could be lower than expected, resulting in higher farm prices and lower deficiency payments. For every 5 cent per bushel decrease in the deficiency payment rate, deficiency payments will decrease by about $100 million.

3. Is USDA presently evaluating options in the event present weather conditions do not improve and if so, what options are under consideration?

Answer: Since the 1930's, we have experienced only four droughts of the magnitude of the one last year. We have never witnessed back-to-back severe droughts. In fact, over the last 20 years, yields of major crops have rebounded to within 10 percent of "normal" following severe droughts, such as in 1980 and 1983.

Nevertheless, USDA meteorologists are carefully monitoring the weather situation across the United states and briefings are being presented on a regular basis to top USDA staff. In addition, weather briefings are being made to Members of the Congress. Also, on a technical level, monthly meetings of the Interagency Drought Task Force are being held to assess the current situation and advise top officials.

Options are limited for changes in the 1989 Wheat Program. Winter wheat is planted and the planting of spring wheat is approaching. The Department is in the process of evaluating alternative program parameters for the 1990 crop in light of the weather problems associated with the 1989 crop.

4. Is USDA prepared to approve state requests for year-long haying and grazing of idled wheat acreage on an expedited basis?

Answer: Procedure is being developed to handle the State requests similar to that of 1988. The county ASCS office will telemail the required information pertaining to the disaster and the need for emergency haying and grazing of the idled wheat acreage to the State ASCS office. After concurrence by the State ASCS office, the county request will be FAXED into the Deputy Administrator, State and County Operations. We are prepared to provide a turn-around time of less than 24 hours following receipt of the request. The decision will be telephoned to the State ASCS office, who shall immediately telephone the county ASCS office. The county ASCS office shall then use the fastest means available to notify the producers in the county.

5. Is USDA prepared to make an expedited decision with respect to failed acreage requests to ensure farmers have options on their 1989 wheat acres?

Answer: Standard operating procedure is in place for the handling of failed acreage requests. Requests for failed acreage must be filed within 15 days after the disaster occurs, but before all evidence of the crop is destroyed. However, county ASC committees must be satisfied that the cause of the failure was indeed a condition beyond the producer's control and that the crop was affected to the extent that it would be uneconomical to harvest.

Questions in Congressman Traxler's letter to Chairman Glickman:

1. First, producers of dry beans in my area have been penalized because ASCS includes in the count of what was harvested cull beans that are not salable. In response to letters from me to ASCS Administrator Milton Hertz, he has maintained that the culled beans must be included in the harvest count because the 1988 Disaster Act does not provide him authority to make "quality loss adjustments" on nonprogram crops. I have maintained that he does have the ability to interpret the term "harvest" reasonably, so that harvest should include only a salable commodity, and not every worthless item brought in with the good.

My concern is particularly amplified by the fact that if ASCS is allowed to continue to maintain this position, then those producers who made an honest effort to harvest what they could will be penalized compared to other producers who might have decided to avoid the harvest and take their chances with the disaster program. This action by ASCS simply sends the wrong signal to farmers.

Answer: The Disaster Assistance Act of 1988 (1988 Act) provided the Secretary of Agriculture with the discretion to provide compensation to producers of program crops and soybeans for quality losses. Compensation for quality losses for non-program crops (e.g., dry beans) was not included in the 1988 Act. Accordingly, there is no authority to make quality adjustments for nonprogram crop losses.

The program crop quality loss adjustment authority had been mandatory in an earlier draft of the bill, but the potential budget exposure led the Conference Committee to make it clearly discretionary. The Department of Agriculture assigned no cost to the provision when the total outlays for the bill were summarized at $3.9 billion. The presumption was that it would not be implemented. To have implemented such a costly provision would have added to the likelihood of a Government-wide sequestration under the Gramm-Rudman-Hollings Act. In turn, this would have taken away part of the assistance made available for drought-stricken farmers under other provisions of the legislation.

It may seem unfair that the quality adjustment provision of the 1988 Act was not implemented; however, other provisions of this legislation are providing producers with considerable compensation to help offset their losses. Certainly, the quality loss compensation would have been helpful, but the cost of implementing this provision would have been excessive.

2. Secondly, as I am sure you know, a number of producers are finding that their harvested corn has been affected with aflatoxin. This discovery is made well after the harvest has been completed, and seems to be more apparent when warmer spring weather returns to farm areas. Southern farmers are learning of the problem earlier than northern farmers, and some of my producers are concerned that they will not know whether or not they have a problem until after the March 31 deadline for disaster assistance has passed.

I am hopeful that there may be some action of an administrative nature that can be taken to allow producers to make application for the disaster program when they could not through any fault of their own have know of the program prior to March 31. When recently testifying before the Subcommittee on Agriculture of the House Appropriations Committee on which I serve, Mr. Hertz seemed to indicate that he did not believe that he had any authority to deal with this possible problem. Anything that you could do to help resolve this matter would be greatly appreciated.

Answer: The deadline for applying for disaster assistance is March 31. However, May 15 has been established as the final date for furnishing production evidence. Producers having concerns about aflatoxin contamination should make an application for benefits prior to March 31 and have a sample of the corn tested for aflatoxin contamination. Should the test prove positive for aflatoxin contamination in excess of 20 parts per billion, the producer has the option to exclude the production for disaster purposes. To exclude the production, it must be destroyed, without feed or other benefit, prior to the May 15 deadline for furnishing production evidence.

3. Thirdly, ASCS has just changed its procedure for the calculation of commodities involving so-called "phantom acres". Farmers who had suffered failed crops last spring were allowed to plant a new crop on those failed acres. The understanding at the time was that the farmer would not be eligible for disaster assistance on those phantom acres if a disaster occurred. This is the calculation that took place until recently.

ASCS has now directed county offices to include the amount harvested on those phantom acres with the total harvest count, while not including the phantom acreage in determining whether or not there were eligible losses. As a result, producers will find that with the inclusion of the harvest from the phantom acres in their total harvest count, they fail to meet disaster loss criteria on their original acres. In essence, the production on the acreage counts, but the acres do not.

We will now find the situation where ASCS will have to go to producers who have already been paid, recalculate their losses, and demand refunds because of the modification of this procedure. If farmers did not expect the phantom acreage to count for disaster assistance, why should the harvest be included in the harvest for the base acreage?

Answer: A producer is allowed to plant subsequent crops on acreage the producer had planted to another crop which failed in the same year. It is specifically and repeatedly provided in the Disaster Assistance Act of 1988 that the provisions thereof are applicable to "the total quantity of the 1988 crop of a commodity that such producers are able to harvest on the farm." Accordingly, if the producer has production on the farm of the same type of commodity as the subsequent crop, the production of the subsequent crop is taken into consideration to determine whether a producer is eligible to receive a disaster payment for the loss of production of that commodity on the farm. However, the production of the subsequent crop does not affect the eligibility of the producer to receive a disaster payment with respect to the crop of some other type commodity which was initially planted but which failed as a result of the disaster. There is, therefore, no statutory authority to exclude the production from "phantom acres" in the determination of disaster benefits for the producers on a farm.

Questions for the record from Congressman Grandy:

In Iowa, the farmers have been getting mixed signals from ASCS and FCIC, needless to say, this has been cause for a great deal of frustration and confusion. The most serious problem arose when ASCS officials would advise farmers that only the farm with the disaster needed insurance, while FCIC would advise the same farmer that all of his farms would now require insurance.

1. Has this problem of miscommunication been resolved, and if so which agency is correct in its interpretation.

Answer: Section 207 of the Disaster Assistance Act of 1988 (the 1988 Act) requires that producers on a farm agree to obtain multiple peril crop insurance for the 1989 crop of a commodity for which the deficiency in production was in excess of 65 percent. This requirement applies only to the farm for which the disaster payment was made. However, FCIC requires a farmer to insure all acreages of a commodity planted within the county. The FCIC provision may require insuring the commodity on several farms. Section 207(b)(4) of the 1988 Act allows a waiver of the crop insurance requirement if the annual premium exceeds 25 percent of the amount of any payment, loan, or forgiveness sought. A producer operating a number of farms may qualify for this waiver if a payment, loan, or forgiveness were received on only one farm.

ASCS personnel should, and we believe in most cases do, explain the FCIC requirement of insuring all acreages of the crop in a county although they are not required by current ASCS procedure to do so.

2. I have received very similar concerns about discrepancies between ASCS and FCIC regarding the crop loss determinations. What efforts have been made to address the inconsistency between ASCS and FCIC measurements?

Answer: County ASCS personnel have been instructed to utilize FCIC measurements when available. However, county ASC committees must assure that the evidence is satisfactory. Any evidence which does not appear to be satisfactory to the county ASC committee must be reviewed and checked. Additionally, reports have been received of evidence being received from two separate reinsured companies that varied. In such cases, it becomes necessary to determine which, if either, is correct.

3. I understand that the number of options available to USDA to respond to the needs of livestock producers during a drought are extremely limited. Last year, in particular, it appeared that you had very few options available to assist livestock producers.

For natural forage animals, such as beef cattle and sheep, you allowed haying and grazing on set-aside acres, haying of conservation reserve program acres, and green cropping of oats. Otherwise, there were only two basic programs to assist livestock producers, the Emergency Feed Assistance Program (which provides CCC-owned grain at 75 percent of the county loan rate) to beef, dairy, sheep, and goat producers and the Emergency Feed Program (which provides up to a 50 percent cost-share on the price of feed) to beef, dairy, sheep, goat, and pork producers.

Other than the Emergency Feed Program that provided for cost sharing of feed expenses, pork producers were not eligible for a program of feed assistance at a specified percent of the county loan rate. They were also not allowed the only other option, which was the harvesting of set-aside acres. Could you please explain why pork producers were not allowed to harvest oats and other crops on set-aside acres, while other livestock producers were given similar options?

Answer: The Agricultural Act of 1949, as amended, provides that the Secretary of Agriculture shall allow the haying and grazing of acreages devoted to acreage conservation reserve (ACR) and conservation uses, except during a consecutive 5-month period established by the State Agricultural Stabilization and Conservation committee, unless it is determined that such haying will have an adverse economic effect. The Secretary also may authorize emergency haying and grazing in the event of a natural disaster. However, we have never allowed the harvesting of oats or other small grains from acreages designated as ACR, other than by haying. To do so would be counterproductive to the purpose of the annual acreage reduction programs.

4. I understand that a livestock producer that fed his own feed first and then fed his purchased feed would be eligible for feed assistance. On the other hand, if a livestock producer in anticipation of a feed shortage because of a drought, kept his own grain in storage and purchased additional feed, but fed his purchased grain before feeding his own grain, is not eligible for emergency feed assistance. Is there any way that we can make this situation more equitable, so that livestock producers who have the foresight to plan for shortfalls in feed are not unnecessarily penalized?

Answer: The question is closely related to the issue of whether the better managers are penalized because their practices of maintaining reserve feed supplies may make them ineligible or reduce their eligibility for assistance. Each producer's situation will be different because of variables such as when the producer filed his application, how much feed was on hand at the time of application, if any of the feed on hand was purchased feed, and the time of such purchase.

Program provisions require that in order to be eligible for assistance, a producer must not only have suffered a substantial loss of feed production, but the producer must also have insufficient feed for eligible livestock for the estimated duration of the emergency. Therefore, all feed purchased for eligible livestock that is still on hand on the date of application is considered feed available in computing the applicant's total allowance. However, within that total allowance, any of the feed purchased after the beginning of the crop year established for livestock feed programs is eligible for cost share.

The present provisions should not be viewed as penalizing producers who plan ahead for possible shortfalls in feed production. Generally, producers who maintain a year's supply of feed on hand made their purchases, if any, at the best of market prices, and by so doing may well enjoy a better margin of profit than those who must depend on emergency assistance during a disaster year.

5. Congress was told that approximately $800 million would be distributed in 1988 and another $800 million would be distributed in 1989, under the emergency feed assistance programs. To date less than $300 million in feed assistance has been made available under the emergency feed programs. Please explain the great discrepancy between the amount of feed assistance projected and the amount actually received by livestock producers.

Answer: The Department's mid-session review budget estimates for the livestock assistance program outlays was $400 million for FY 1988 and $600 million for FY 1989. The original estimates on emergency livestock assistance were made in July and August 1988 during a time when the summer drought was not expected to improve. The August estimate for corn published by the National Agricultural Statistics Service (NASS) was 4,479 million bushels. As crop conditions improved, NASS later raised their estimate of the corn crop to 4,921 million bushels, almost 10 percent higher than the first estimates in August. In addition the Pasture and Range Condition Index, a measure of range and forage conditions, has increased more than 30 percent since July 1988. Improved crop and pasture conditions translate into a lower crop loss suffered and more feed on hand by eligible livestock producers and, hence, lower payments under the emergency livestock programs.

The original budget projection did not reflect the statutory requirements that if a producer suffers a crop loss which would allow benefits under both the emergency livestock feed assistance provisions and the 1988 disaster payment program, the producer may not receive benefits for the same loss from both programs. At the time the estimate was prepared the statutory requirements had not been finalized. Moreover, there was no clear basis for determining how many producers may be affected. This technical adjustment reduced estimated outlays for emergency livestock programs by $115 million to $173 million.

Since the majority of livestock producers could qualify for assistance under either the feed assistance or disaster payment provisions, many eligible livestock producers deferred taking the feed assistance until they could compare the potential returns from the two forms of assistance. Substantial amounts of loss are still outstanding for which feed assistance may be required by eligible applicants, but it appears more producers than anticipated have elected to receive cash payments rather than feed assistance for their crop losses.

6. I also recall that the Department of Agriculture told this Committee that it would cost an additional $2 billion to provide feed assistance to those livestock producers that did not produce their own feed. Please explain how this could be mathematically possible, if livestock producers that produce their own feed comprise at least half of the livestock in this country, received less than $300 million in feed assistance?

Answer: The original estimate of an additional $2 billion to provide feed assistance to those livestock producers who did not produce their own feed was based on the original estimate for feed assistance to those that did produce their own feed. As mentioned in the above question, that estimate was $1.6 billion over the 1988 and 1989 Fiscal Years. Expanding the program to include livestock producers who do not produce their own feed significantly expands the number of eligible producers. In addition, the amount of assistance which would be necessary to be made available to producers who do not produce their own feed increases disproportionately to the number of producers who are eligible. By definition, producers who do not produce their own feed cannot show a 40 percent crop loss before they become eligible for assistance, as is required for producers who do produce their own feed. Accordingly, our estimates were based on the assumption that producers who do not grow their own feed would have been eligible for an additional 40 percent of grain under emergency livestock assistance programs. Hence, the additional $2 billion estimate was based on a larger baseline estimate ($1.0 billion instead of $300 million), and on a significantly larger number of potential bushels of assistance necessary if the program had been expanded to include producers who did not grow their own feed.

General Comments on Feed Assistance Estimates

Feed assistance needs were estimated as follows: Total population of eligible livestock species were estimated by State. Feed needs for the estimated livestock population were adjusted for counties not declared eligible, crop loss, feed on hand, producers who do not grow their own feed, and the effects of payment limitations. The eligible animal population was also translated into feed needs by assuming 10 pounds per animal unit per day for 9 months. Emergency livestock assistance was given on the lesser of the feed needs or feed loss.

7. I understand that historically provision has been made for helping livestock producers who are experiencing severe water shortage situations. Specifically, cost-sharing assistance is made available for construction or deepening of water wells for producers and livestock in desperate need of water.

I notice that the regulations for eligibility for water assistance essentially restrict assistance to water wells in fields that are not located near any farm buildings.

I understand that there may be concern about potential abuses by farmers using this program to supply domestic water needs to their own family rather than for the purpose of providing much needed water to their livestock. Presently, the water assistance program is limited only to grazing livestock and not available to hogs or dairy cows contained in a barn. It appears there ought to be some way to make the water assistance program equitable. I ask you to reevaluate the water assistance program, so we can avoid any discrimination between livestock species, but more importantly provide much needed water to suffering animals during a drought.

Answer: The purpose of the Emergency Conservation Program (ECP) is to return agricultural land to productive agricultural use after it has suffered severe damage as a result of a natural disaster, such as a flood. Under the ECP, cost-share assistance with respect to emergency water conservation or enhancing measures carried out during periods of severe drought has been made available to livestock producers only in connection with the raising of livestock under pasture conditions because of the effect the drought has on the pasture. Livestock confinement operations are not affected by pastures drying up because of drought. Since limited program funds are made available for ECP, the Department is not in a position to expand the program to make available cost-share assistance for confinement operations for livestock.

Questions for the record from Congressman Stenholm:

1. There have been concerns raised about the level of feed assistance that has been made available for livestock under the Emergency Feed Assistance Programs, as implemented by the Department. For example, it is my understanding that a mature sow is allowed 3.3 pounds of feed assistance per day and for any other swine less than 6 months old, they are allowed a ration of only 2 pounds per day. What methodology was used in establishing your current daily feed ration allowance guidelines? Do the guidelines take into account varying livestock maintenance requirements?

Answer: Section 603 of the Agricultural Act of 1949 as included in the Emergency Livestock Feed Assistance Act of 1988 states that the Secretary of Agriculture shall provide emergency feed assistance for the preservation and maintenance of livestock. A beef cow has been determined to be the basic animal unit, and the amount of feed needed to preserve and maintain 1 unit has been determined to be 10 pounds of feed grain equivalent per day. Comparable feed needs have been established for other types of livestock and poultry based on their age and feed needs under average climatic conditions. These allowances have been established to preserve and maintain livestock; they are not intended to provide optimum nutrition for weight gain or milk production. The current nutritional requirements are based on Frank Morrison's work as published in "Feed and Feeding ".

We are currently reviewing the level of feed assistance made available to the various types of animals. In the review we will look very closely at the nutrient requirements as established by the Committee on Animal Nutrition, Board of Agriculture, National Research Council.

2. There have been concerns raised surrounding disaster assistance received by multi-species operations. More specifically if a producer has several hundred hogs and his children have several 4-H cows as club projects, is the livestock producer denied eligibility for feed assistance because of hay or pasture grazing availability on his operation?

Answer: A producer who has several hundred hogs, who lost 40 percent or more of his 1988 feed crop production, and whose cattle consisted only of several 4-H cows as club projects for children would not likely have enough hay and pasture on hand to be denied eligibility for feed assistance unless it was being produced for sale as a cash crop. If the producer has a substantial excess of hay or pasture produced on the farm over the amount the 4-H cows can use and if the producer's cattle feed was not damaged by the drought as much as the hog feed was, the amount of assistance to purchase hog feed might be reduced. However, if the pasture and hay were also damaged, the producer could receive even more assistance to purchase feed for his hog operations.

Livestock producers who are exclusively hog producers need not include pasture or hay crops as feed available for the hogs, but neither can a loss be considered on feed crops not included as feed for eligible livestock.

We receive basically the same complaint from hog producers who raise only hogs and an excess amount of corn. These producers state that not all their corn should be considered as feed for their hogs because they raise that excess corn as a cash crop just as they might raise alfalfa as a cash crop.

3. Will livestock producers, that have both hogs and cattle, be eligible for feed assistance for their hogs until the next crop becomes available in the fall of 1989?

Answer: A livestock producer with both hogs and cattle will be eligible for assistance for hogs until grain crops become available provided that, at the end of the 1988 livestock feed program year established for the county, (1) the producer has an unused feed loss remaining from the 1988 crop year, and (2) the total feed on hand in pounds of feed grain equivalent for both types of livestock does not exceed the total feed needs for both types of livestock.

4. Do you have a current detailed assessment of the amount of assistance that was made available to livestock producers (both tonnage and dollar amount)--broken down by individual species?

Answer: The amount of assistance made available is reported for total eligible animal units, but is not broken out by species of livestock. As of February 28, 1989, cost-share assistance totaling $273,732,474 was paid with respect to 3,678,418 tons of feed for 15,711,327 animal units. In addition, 3,102 tons of CCC-owned feed grain have been sold to livestock producers at 75 percent of the county loan rate, representing additional assistance valued at about $12 million.

5. It is my understanding that eligible livestock producers must reapply for disaster assistance each feeding period. How much paperwork must a producer complete when re-applying for each feeding period in order to receive full benefits? What is the rationale for requiring numerous re-applications?

Answer: Livestock producers must complete a CCC-642 for each feeding period. A feeding period begins on the date the producer applies and ends the earlier of the date feed next becomes available for the type of livestock or the end of the crop year for livestock feed payments. An alternate method is provided for situations where there would be a number of short feeding periods. In most cases, producers need only file one CCC-642 during the current crop year, and one in the subsequent crop year if they have unused feed loss left over from the current crop year. We feel a minimum of one application is needed per livestock feed program crop year because producers frequently change livestock numbers and types of livestock feed. Without this requirement, producers could lose eligibility resulting from operation changes, and CCC would have a very difficult time trying to maintain compliance with the law as established by Congress.

QUESTIONS FROM CONGRESSMAN TIM JOHNSON
AFTER HEARING MARCH 23, 1989

Honey production

I exchanged correspondence earlier with the Department on their resistance to including honey producers under the crops portion of the Disaster Assistance Act., USDA is contending the according to the legislation, relief is calculated by determining acreage planted and production harvest, and this cannot be done for honey. I would maintain that this is totally baseless because honey producers currently submit to their county ASCS offices for the purposes of participating in the honey loan program, the number of colonies derived from an acreage and the amount of production obtained from those colonies. If this is not the case, I would like to ask how FmHA determines honey losses for disaster loans, since it is my understanding that honey production losses are eligible for disaster loans. The honey production in my state of South Dakota was basically cut in half, from 33.5 million pounds in 1987 to a little over 18 million pounds in 1988. The same is true of the other major honey producing states of North Dakota and Montana.

USDA also contended that losses in egg and wool production could not be included either, but I would counter that both poultry and sheep are eligible for the emergency feed programs, which honey producers are not.

ANSWER: The availability of disaster assistance under Title II of the Disaster Assistance Act of 1988 is based upon the loss of a specified quantity of the 1988 crop of a commodity that is determined by taking into consideration the sum of the acreage on a farm planted to harvest. While the producer of the crop which is the pollen source that is planted on the farm may be eligible to receive a disaster payment with respect to loss of production of the crop, there is no basis upon which to make disaster payments to honey producers.

Crop insurance proceeds counting as feed on hand

You indicated during the hearing that a rulemaking process was underway to make this change. Why have you waited so long to do this, especially in light of the fact that you indicated that producers would be able to go back and have their emergency feed applications adjusted to reflect that crop insurance proceeds would not count as "feed on hand?" How difficult would it have been to issue regulations on this immediately after the disaster bill was passed. Is there an effective date already in place that would be the deadline for producers to have their emergency feed applications amended or would you establish a date within these new regulations?

As you well know, the ending date for signing up for the livestock programs is March 31, 1989, although it is my understanding that the Secretary has the ability to change this. Has there been any discussion of extending this deadline in light of the continuing dry conditions in many parts of the country?

ANSWER: The issue concerning treatment of multi-peril crop insurance payments in determining eligibility for feed assistance is currently under consideration with other issues included in the final rule to be published for the livestock feed programs. If a policy change is made, the determination will include the establishment of an effective date for the change.

Livestock feed program provisions preclude the need for extending the deadline for filing applications. Producers receiving assistance for 1988 losses can continue to receive such assistance, within the limits of their eligibility, until the end of the crop year for the livestock feed programs. The beginning of the new crop year is the date grazing normally becomes available in the spring, as determined by the county Agricultural Stabilization and Conservation committee. Some producers will be eligible for assistance after the end of the crop year. These are producers who have not received assistance to the full extent of their 1988 loss and whose feed needs for eligible livestock exceed feed on hand.

If drought persists into the next crop year, requests for implementing the program for 1989 can be considered as soon as 1989 losses can be documented.

Advanced deficiency paybacks from 1988 crop year

I have had several producers ask me about the payback of advance deficiency payments from 1988. I realize that producers who may have to do so have until July 31 of this year, but I would simply like to clarify the situation facing wheat and feed grains producers for the record.

ANSWER: The 1988 disaster payments that producers received were authorized by provisions of the Disaster Assistance Act of 1988 (the 1988 Act). Section 201(a)(3) of the 1988 Act provides that the total quantity of a crop of a commodity on which deficiency payments otherwise would be payable to producers on a farm under the Agricultural Act of 1949 (the 1949 Act) shall be reduced by the quantity on which a payment is made to the producers. Accordingly, producers will not earn final deficiency payments on the quantity of lost production for which a disaster payment was made. The 1988 Act further provides that the refund of the advance payment may not be requested before July 31.

Section 107C of the 1949 Act provides that producers shall refund at the end of the marketing year unearned advance deficiency payments, including unearned increased established price payments (commonly referred to as "Findley payments"), which producers had received. In order to be certain that producers are aware of this requirement, paragraph 16 of the appendix to the contract to participate in the 1988 commodity price support and production adjustment programs provides that "A person shall refund to CCC any amounts which represent a payment that exceeds the amounts of payments actually earned under the 1988 programs for wheat, feed grain, upland and ELS cotton, and rice." The end of the 1988 corn marketing year is August 31. The end of the 1988 marketing year for oats and barley is May 31. Accordingly, refunds of unearned deficiency payments are due at such time.

The 1988 Act provides different benefits under the emergency feed program and the crop disaster program. Section 211(b) of the 1988 Act prohibits the making of benefits to a producer under both programs for the same loss of production. If a producer is eligible for benefits under both programs, a comparison may be made to aid in deciding which program benefits are best for the specific operation. In no instance, however, may a producer receive benefits under both programs for the same loss of production.

Cultural practices

I have had several concerns voiced to me in this area, but I want to raise only two, the first of which deals with alfalfa seed producers who harvest their first growth as hay to promote better seed quality. One particular case involves irrigated producers who cut their first growth and made less hay than they had received in past years. Now it appears that these producers are being deemed ineligible to receive compensation on their lost seed production. They have also been told that they would not be eligible to receive disaster assistance on their lost hay production if they decided to go that route instead. I will be sending you the specifics of this particular case, but I did want to bring you attention to the situation where the county and state committees may agree with the cultural practices used, but they are bound by what is contained in the ASCS handbook.

I have another case where a producer practices sustainable agricultural methods, and he appears to have been penalized because the county committees may not be familiar with some of the practices and in this case, there is no appeal available. I would encourage you to help out the folks on the local level by allowing them to take into account work that has been done by our land grant universities and other groups in this area.

ANSWER: A crop normally harvested for both hay and seed is eligible for disaster payments on the hay loss if only hay is harvested and other eligibility requirements are met. If only seed is harvested and other eligibility requirements are met, the crop is eligible for a seed loss payment.

In responding to your second question, we assume you are referring to organically grown crops. Growing crops organically is a production practice rather than a different variety of the same commodity. There is no statutory authority to consider organically grown crops differently than those same crops grown in a conventional manner.

Mr. Glickman. Mr. Dyson.

Mr. Dyson. Thank you, Mr. Chairman. Let me take the opportunity to thank you and this subcommittee and this entire committee for the help you did provide in the Disaster Assistance Act of 1988. The district I represent has really experienced about three of the droughts, and the Congress reacted when the country as a whole experienced the major drought. I was in that last vote walking over to the Chamber with my colleague from Missouri and we were talking about the situation we think we are going to face again which is another major drought. He is seeing it in his district, and although we are getting a lot of rain of late, I do not think it is going to be quite enough.

So in some point in my period of questioning I would like to know what your reaction is going to be to that, if we either come up with legislation or you send a package down to us. Before that though I would like to offer a question, in fact, I would like to restate a question that my colleague from Indiana, Mr. Jontz, had asked about corn that has been infected with aflatoxin. You know that is now eligible for disaster assistance. He talked about the deadline. You talked about the deadline which is coming up in just a couple of days. As you obviously know, farmers are having problems that they may not have checked their corn that they have put in storage. In fact, I think one of you said that probably what they ought to do is probe their bins, and in the same breath you indicated that probably would not be enough of looking into this problem.

We in Maryland, it is my understanding, the University of Maryland, I think, has been testing for farmers, for our State farmers. Are other States doing that and my question and Mr. Jontz' question, are you going to provide some kind of flexibility in that in the Department?

Mr. Hertz. As I commented earlier, Congressman, we would like to get a sunset to this program and get it behind us. The legislation specifically provided that sign up time would end March 31. The May 15 date was established to give farmers 45 days to bring in whatever evidence to support their claims. We would like to stay with that date and my reference to the probing, farmers tell me that aflatoxin can be contained in a very small pocket and does not necessarily run through the whole amount of grain. And we feel that it is not accurate and they still may have it at some point in time when they deliver it.

Mr. Dyson. Are other States offering the service that the University of Maryland is offering in Maryland?

Mr. Hertz. I am not aware, but I would presume that most land-grant institutions or experiment stations would be quite involved in the, given the scare of the aflatoxin, they would be involved.

Mr. Dyson. One of the things I hear again and again in my district and I assume a lot of others because listening to Mr. Marlenee talk about the complexities to sign up, one of you said the forms were too complex. We constantly hear this all the time. In appealing the appeal process that the farmer goes through, he goes to the county committee, that only meets once a month. If he is turned down, the next appeal is to the State committee, that only meets once a month. If that happens then he still has failed in this process. He then has the right to appeal to Washington.

This obviously is very burdensome. Is anything being done to try to make that a little bit less burdensome?

Mr. HERTZ. An appeal is usually generated when a producer feels that he has been, so to speak, harmed by some action that the ASCS has taken for his failure to fully comply with some provision of his contract and the program that he is involved with. We feel that the administration of the county offices with their elected county committeemen meeting once a month can take care of that business, and again, with the State. It is an ongoing process here in Washington, if they should come that far.

Mr. DYSON. Do you not hear complaints on that?

Mr. HERTZ. We hear complaints when we are not timely, that is true. Not necessarily at the county or the State level, probably more here in Washington.

Mr. DYSON. I see the red light is on, but let me go back to that original question. What is the Department doing in reaction to the potential of another drought?

Mr. HERTZ. Congressman, if you remember last year starting in about mid-February, ASCS kind of took the lead that eventually became a departmentwide project in monitoring areas of the country that had the appearance at that point in time of having some weather problems, starting with the Pacific Northwest and a couple of areas in Texas. We are doing that same thing again this year. That we are asking through our ASCS system to provide us with reports that would indicate that the wind is tearing grain out of the ground in 18 counties or 14 counties or half the counties, that we know where we are. We have moisture records. We have reports on conditions of crops. And we can be prepared much more to react to the request to implement the programs that we do have on the books that would relate to emergencies and disaster kinds of programs.

Mr. DYSON. When are those figures available?

Mr. HERTZ. They are updated weekly.

Mr. GLICKMAN. Mr. Hertz, I just have a couple more questions and I think Mr. Volkmer does. I will try to get you out of here in about 5 minutes. And anybody else who does, as well. I want to go back to the aflatoxin issue. We will be holding a hearing where we will be hearing from both USDA people, as well as outside scientists, as well as people developing equipment in order to test for aflatoxin.

Based on the amount of indemnity payments made to date, your opinion is that it is not been the problem as first feared in terms of size and scope?

Mr. HERTZ. That is true. The size and scope on the aflatoxin problem has been much much smaller than what at least the media would suggest that it is.

Mr. GLICKMAN. Some of the concerns that have been expressed to me is that our testing capability for aflatoxin is rather antiquated and impaired and therefore may not accurately reflect the amount of aflatoxin that is out there; do you know if your folks have looked into this?

Mr. HERTZ. In ASCS we have not got involved in any of the testing. We felt that it would be more appropriate for the Federal

Grain Inspection or the private sector of the elevators and warehouses to do that for us.

Mr. GLICKMAN. But from your perspective in terms of payments made, it has been a smaller problem than you had thought it was going to be?

Mr. HERTZ. Much smaller, yes.

Mr. GLICKMAN. I want to ask you a bit about crop insurance. What is ASCS doing to encourage people to buy crop insurance for this crop year, the 1989 crop year, in light of what we foresee as a possible drought reoccurring?

Mr. HERTZ. To the extent that we have been involved in making disaster payments and that the farmer has above a certain percentage of loss, he is required to buy the crop insurance, we worked with our sister agency in making sure that their posters and their advertising and their awareness program is displayed in our offices.

Mr. GLICKMAN. But you are the ones that are making the payments? You are the ones that the folks are dealing with more than the Federal Crop Insurance Corporation, and I would just hope that you would be an active participant in letting people know that that is available for them, at least for Winter wheat producers. Who would still be eligible for crop insurance?

Mr. VON GARLEM. Most of the spring seeded crops.

Mr. GLICKMAN. Winter is gone, you are correct. I would ask you one other question. Sodbuster—one of the problems I am having has to do with farmers, particularly tenants, their landlords have basically told them, you must sodbust or you must plant in the following fashion. In order to keep their lease, they do it. And I have got a couple situations where those same tenants farm land owned by other people who comply with sodbuster, and that poor tenant is in the Catch-22 situation of being ineligible for disaster assistance on everything he farms, because one of his landlords is being unkind in terms of dealing with sodbuster; is that the way you understand the law to read?

Mr. HERTZ. Yes. I believe the law provided that there would be cross-compliance on all producers, as it would cross landlord, tenant, other farm units, that each individual would be involved in. If you mess up on one, you messed up on all of them.

Mr. GLICKMAN. What recourse does the tenant have, though against the landlord who runs the show and controls the shots? That is not fair. Does he have any under existing agricultural law?

Mr. HERTZ. Not that I am aware of, sir.

Mr. GLICKMAN. So he would have to find some other theory of law in terms of the lease, but as far as you are aware that tenant is stuck, he cannot get disaster payments?

Mr. HERTZ. As long as he would be a party of the contract that he would have with ASCS, yes.

Mr. GLICKMAN. What about the landlord. I understand it does not work both ways. Let us assume, for example, that that landlord has one tenant that he says, you must sodbust, then he has got nine other parcels that he does not make that requirement on. Those tenants can collect disaster assistance, cannot they—assuming they go directly to the tenant?

Mr. VON GARLEM. He can, too.

Mr. **Glickman**. He can too on the other ones. So what we have is the tenant who is victimized is absolutely stuck, but the landlord is not; why do we do that?

Mr. **Von Garlem**. Because there is a specific exemption for landlords in the sodbuster law.

Mr. **Glickman**. Now apart from that, in your judgment is that fair the way it is done?

Mr. **Von Garlem**. We try not to spend too much time talking about fairness. We try to implement the law.

Mr. **Glickman**. Mr. Von Garlem, you helped implement this law. We have got to know what to do. If this is not right, then our job is to change it. Is it fair to put the burden on the tenant when there is not a comparable burden really on the landlord?

Mr. **Von Garlem**. Personally, I questioned that, but my question and 50 cents will get you a cup of coffee.

Mr. **Glickman**. Not anymore, it is 85 cents down here.

Mr. **Von Garlem**. In all sincerity, that was something that was debated heavily and it was a specific exemption written in the law for landlords.

Mr. **Glickman**. In addition, some of the points that Mr. Volkmer has raised, this seems an issue of equity that is not right, and I have tenants out there who are hitting their head against the wall. They do not understand why the offending landlord can do whatever he wants to do and get payments and the tenants cannot.

Mr. **Von Garlem**. He can get payments in other forms.

Mr. **Glickman**. But the cross-compliance does not apply to him, it applies to the poor tenant who sometimes is not in a position to bargain. That is what may have been our fault in Congress. We did not recognize the improper bargaining relationships between the landlord and tenant in that thing.

That is all I have. I know Mr. Volkmer had another question.

Mr. **Volkmer**. Yes, I want to get back to my favorite topic. First I want to apologize for using the word stupid. I want to apologize for that. I know you are not. But this is a form, a two-page and there is a work sheet that the farmer turned in. This is a computer printout and I cannot find where that much extra work is going to be. All of the information is on here that you need to make the determination as to the eligible feed for the eligible type of livestock.

But my other concern is this, and I did not ask it before. I talked about hay. I did not talk about pasture. Is pasture included too?

Mr. **Von Garlem**. If he has a class of livestock that uses pasture——

Mr. **Volkmer**. Wait a minute, I have my cows over here; I have my hogs over here; I have pastureland over here; I have hay in the barn; I have corn in the silo; Now does all of that put together, including the pasture?

Mr. **Von Garlem**. Yes, sir. If there is a class of livestock on the farm that use pasture, yes, sir.

Mr. **Volkmer**. That is all put together?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. Have you ever seen hogs out to pasture?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. You have?

Mr. **Von Garlem**. Yes, sir.

Mr. **Volkmer**. Where?

Mr. **Von Garlem**. When I was growing up, I had mine on pasture.

Mr. **Volkmer**. You put your hogs on pasture?

Mr. **Von Garlem**. Yes, sir.

Mr. **Newcomb**. If I may, producers in the Southeast who only have hogs, have given us trouble because we do not count pasture because they say they actually pasture their hogs.

Mr. **Volkmer**. They pasture their hogs?

Mr. **Newcomb**. Yes, sir. And that is one of the problems, how to determine what type of feed is suitable for what livestock.

Mr. **Volkmer**. I will wait for the person from Iowa to testify. My hog producers—I have never seen them put hogs to pasture. I never have. I have seen cattle on pasture, but I have never seen hogs on pasture. I have seen hogs out in hog lots. There is not anything left after a year. When it rains it is mud, but it does not, it is dirt. There is no pasture out there. I just wanted to know if you counted it.

One thing I want to ask you to do. Since you do not seem to understand what I was trying to say when I wrote this language in the law, I want you and the General Counsel to write the language. You know what I understood now, right? What I wanted to do; is that correct? From my discussions, you understand that I do not want hay in pasture to go for hogs? I want you to write the language and get it to me, that does what I think I did. Do you understand? So that when it does go into law, you will understand it. Because you will have written it. Do you understand that? I would like to have that by April 6. Thank you.

[U.S. Department of Agriculture's response follows:]

Officials of the Department of Agriculture, including representatives from the Office of the General Counsel, are available to meet with you to draft the specific legislation which you desire. In order to facilitate the drafting of such language, we suggest that Counsel for the Committee on Agriculture also be present.

Mr. **Smith**. Would the gentleman yield?

Mr. **Volkmer**. Yes, I will yield. Maybe, you should do the same thing, the gentleman from Oregon, on your problem.

Mr. **Smith**. Thank you for yielding. The only hogs that pasture are my neighbors hogs who pasture on my ground.

I just want to add one other thought to my question about drought eligibility. I want you to look at the conference committee report on the 1988 act which has in it a sentence which I do not have in the law. The sentence that was stricken from what I gave you reads: "Or at the producers option for assistance under such preexisting programs." The point simply is they might not have qualified for the 1988 program, but at the producers' option, they could qualify for drought assistance under the old act which may be a different set of numbers, but still qualify. And I would hope that you would take a look at that because that is in the conference committee report, not in the paragraph that I read to you in 605. So it may be they are eligible under the 1949 act for assistance which may be much different in compensation for drought, than the 1988 act, but it seems to me they cannot be denied if they make that choice.

I thank the gentleman for yielding. Will you take a look at it for me?

Mr. **Glickman**. Mr. Marlenee.

Mr. **Marlenee**. Mr. Hertz. You have heard the questioning and the comments by the members of this committee. You and I have spoken before about the complexities of the sign up in the program. Some of it because of the actions of this committee and the full committee and Congress itself, we have got to admit that we can all share the blame. But nonetheless, the fact is that the American producer is looking at us with some disdain, by the laughing stock of the American producer community. Do you have it within your authority—first of all let me ask—do you consider the sign ups and the burden complex, given the fact that some producers have 64 pages or 64 different forms that they have got to fill out, given the fact that you have to have an appointment to get work done, to go into the office to sign up or to deal with crop insurance or deal with the other program of disaster payment, you have to have an appointment. Do you consider the regulation a burden?

Mr. **Hertz**. Certainly there is complexity and there is a requirement to fully implement the laws that we are required to administer, Mr. Congressman, and alluding to the appointment, some offices use that as a management tool to not have farmers stacked up for half a day. That is an arrangement and it works very fine. I probably should state another example. When we visited about 2 months ago about your concerns and all the requirements placed on the farmers to make the personal determination, we went back and checked and one of the counties in your State was the county committee and it probably refers to what Mr. Jontz was saying, in the inconsistencies from one county to another, were asking for material that they did not even know what to do with—were way out of line. And I think those are the individuals in that particular county that would be terribly angry and terribly upset. And we feel that we are not doing more than we have to do to administer the law.

I know that in the last 18 months, I have appeared a couple of times in this room, a couple of times on the Senate side, and the administration of the personal determination of the $55,000 payment limitation was supposedly in total shambles. A new law was passed and I think that we had enough direction to say, well all right we are going to administer this law. We are going to take away these ineligible payments that we have been making forever. And it does have adverse impact on American producers. And I think I can say too, relating to that law, that next year at this time or prior to sign up, if there is no subsequent change in that producer's farm operation, he signs and certifies that that is the case and he is finished. There is nothing more to do.

Mr. **Marlenee**. I maintain that the paperwork burden is unduly complicated and it is far too complex; requiring in some cases leases; requiring in some cases, financial statements; requiring in some cases, minutes of meetings that have taken place. And I do not think you as an individual entrepreneur would ever stand still or going into a Government office, laying out before them your income tax return.

Mr. HERTZ. You do not have to furnish income tax returns, if you do not want to.

Mr. MARLENEE. I do not think you would. Your income tax returns would stand still for laying out your leases in a county office in front of all of the Government workers there, laying out your corporate minutes, laying out your financial statement, particularly when the person dealing with you or the one right next to that person may be in competition with you for an additional piece of land or in some other business endeavor. I think it is wrong.

My question to you is do you have the authority within the Department to put together a committee composed of producers and county committeemen from various areas to suggest to you, how you could simplify the sign up and the paperwork procedure?

Mr. HERTZ. We would have the authority to do that, yes.

Mr. MARLENEE. I would request that the Department of Agriculture address this problem immediately and utilize such a committee. Because if you do not, we are going to do it for you.

Mr. HERTZ. Let me say, Congressman, that we have an ongoing program as far as our management. That we have a rotation of county office people that are coming into Washington on a regular basis and work with the program people in working up forms in bringing that county office experience to the program people here.

Mr. MARLENEE. Mr. Hertz, most of these people feel intimidated. Most of the State directors receive their directives from the top down. They are told you will do this, and you will do that. And they are sent to training workshops. Some of the county State committees are sent to training workshops. They receive a mandate from the bureaucrats to carry out the programs.

And what I am trying to tell you is put together a committee and allow them to work and to suggest changes in the program. I am asking you to do that.

Mr. GLICKMAN. I have one last question. Mr. Hertz, last year's disaster assistance package included a requirement that farmers who suffered a 65 percent loss purchase crop insurance, with the provision that the county ASCS could waive that requirement in certain cases. Can you tell us what percent received waivers and what measures were taken to insure that this provision was administered consistently and equitably?

Mr. HERTZ. Off the top of my head, I could not tell you how many waivers have been granted, but I would say it is very very small.

Mr. GLICKMAN. Could you try and find that out for us as well?

Mr. HERTZ. I sure will.

Mr. GLICKMAN. We thank you very much for your testimony today, and we hope that you get back to us on the specific questions that have been asked, particularly the ones that I have requested on the wheat issue for the April 6 hearing. Because by that date, we should have a reasonable idea what the wheat crop is going to look like and we can know if we should move ahead on some supplemental legislation. It would be my intention, I would just say, that if in fact the wheat crop does not improve, and it looks like it is going to be widespread, I would want to move ahead with some comparable legislation like what we passed last year. That is, that Congress should consider comparable legislation and you might let the folks in the Department know that I would hope they would work with us on that. Because I think we are going to have to do it.

Mr. **Hertz**. Certainly, Mr. Chairman, not being able to speak for the Secretary, but given the bipartisan in the Department level of cooperation, I would highly presume that the Department would not try to look in the way of somebody's grief because of a crop loss and that we would cooperate and work with you.

Mr. **Glickman**. I have not talked to Chairman de la Garza about that, but I am sure that he would probably take the lead on that, and I am sure he would agree with me on that as well. Thank you very much.

We next have a panel of Mr. Rivinius, I think, if I got the name right who is secretary-treasurer of the National Association of Wheat Growers from North Dakota, and we have Mr. Bill Nelson, executive director, Texas Wheat Growers Association, Amarillo, Texas.

We appreciate the fact that you have waited so patiently. It is not often that we get the guy who runs the ASCS program before us, so we thought we needed to kind of chisel away at him a little bit. Why do you not go ahead and start and then we may have to stop in a few moments.

STATEMENT OF RON RIVINIUS, SECRETARY-TREASURER, NATIONAL ASSOCIATION OF WHEAT GROWERS

Mr. **Rivinius**. Thank you, Mr. Chairman, and fellow committee members. I want to thank you for the opportunity to present views of the North Dakota and National Wheat Growers Association on the implementation of last year's drought assistance legislation.

I am Ron Rivinius, the wheat producer from Elgin, North Dakota, and a past president of the North Dakota wheat growers.

Mr. Chairman, wheat farmers in North Dakota are very appreciative of the congressional response to the devastating drought that we experienced in 1988. You will recall that crops in the Northern Plains States were hit by the drought long before it spread to the Corn Belt areas. Obviously, this meant that our troubles began earlier and our anxiety built as we looked for relief measures to be taken. In this regard, we also want to acknowledge the attention given to our problems by the Congressional Drought Relief Task Force, and the Interagency Drought Policy Committee which was established by the administration. The direct and sincere concern which was shown to the drought gave us some help in keeping our spirits up.

There is a problem in the implementation of 1988 drought assistance which adversely affects many growers in North Dakota and probably significant numbers in other States. The problem stems from a failure to provide balanced treatment with regard to loss appraisals.

In early July the Federal Crop Insurance Corporation issued a Special Appraisal Deviation for wheat, barley and oat producers in designated counties. Under this policy the crop insurance adjustors were authorized to count only appraised production in excess of 3 bushels per acre in determining yield losses, effective July 5, 1988.

The Disaster Assistance Act of 1988 provided the Agriculture Secretary the authority to take similar steps regarding de minimis yields in making disaster payment determinations which have since been implemented.

As I explained, crop losses in my State were known early. In fact, many crop insurance appraisals were made prior to July 5, when the new FCIC policy went into effect, and growers in this category have not been afforded the same treatment as those whose crops were appraised later. Further, these same producers have had their ASCS disaster payments reduced, due to the fact that FCIC appraisals used for crop loss evidence did not allow for the special appraisal deviation after July 5.

Our farmers have been told that they could seek a readjustment of their yields if their grain is still standing, but that, of course, is impossible since these acres were disposed of 9 months ago based on good farming practices, including weed and insect control.

We hope that steps can be taken to assure balanced treatment of growers suffering 1988 crop disasters, and we would appreciate any help that this subcommittee might be able to give us.

Although hope springs eternal for farmers again this year, I would be called a fool back home if I did not share my concern with you about what I hear when I stop at my local implement dealer; talk to my banker or visit at the coffee shop; the concern is very real in Kansas right now, which looks like another drought year.

In North Dakota, we have had some snow in varying amounts, but nowhere is it sufficient to replenish subsoil moisture. If we do not get spring rains, it just looks like a bad year.

With talk about a Disaster Assistance Program that will not be available and with Federal crop insurance not being improved to cover our basic production expenses, farmers in my area will be hurting very badly. And I would urge Congress to consider extending the Disaster Emergency Program for 1989.

That will conclude my remarks, and I will be pleased to answer any questions.

Mr. GLICKMAN. I think what we are going to do is stop now. Mr. Nelson, I know Mr. Sarpalius wants to come back and introduce you. For the record, we have a vote, so we will do it as fast as we can.

[Recess taken.]

Mr. GLICKMAN. Go ahead and proceed.

STATEMENT OF D.G. "BILL" NELSON, EXECUTIVE VICE PRESIDENT AND CHIEF ADMINISTRATIVE OFFICER, TEXAS WHEAT PRODUCERS ASSOCIATION

Mr. NELSON. Thank you, Mr. Chairman. I am Bill Nelson. I represent the Texas Wheat Producers Association. While we are members of the National Association of Wheat Growers and other groups, we are sticking within our own administrative responsibility of the situation in Texas, as related to last year's and this year's drought.

Instead of addressing the entire drought legislative program last year——

Mr. **Glickman**. Why do we not stop, Mr. Nelson, for one second. My colleague from Texas, a new and very effective member, has come in. Why do I not let him say a couple of words. We just got started.

Mr. **Sarpalius**. Thank you, Mr. Chairman. I apologize for running a little late, but I am very honored to have Mr. Nelson with us today. I have known Mr. Nelson for many years. He has done a very effective job with the wheat producers in Texas and has a very good understanding of the problems that we are having throughout the State of Texas, especially within the Texas Panhandle of the drought problems that we are currently having. I ask him to come before our committee to kind of give us a little overview of some of the drought problems that we are currently having.

We were fortunate enough not to suffer as much last year, as other parts of the United States did. But we sure have some problems this year. And Mr. Nelson, we are very honored to have you come up here and join us today, and look forward to listening to your remarks.

Mr. **Glickman**. Go ahead and proceed, Mr. Nelson.

Mr. **Nelson**. Thank you, Mr. Chairman. We are pleased to have our home town Congressman on this committee. He represents producers throughout the State, and Congressman Sarpalius is on this particular committee. As to the 1988 drought program, the only comment I would like is to commend this subcommittee and its individual members for getting the words drought-related into last year's drought bill which allowed the producers in Texas that had over 100 percent rainfall at the July 5 drought time, but yet they had had severe losses to early drought back in January and February which caused weakened plants that allowed disease and insects and other maladies to cause a total crop loss in many areas.

That made the drought program effective to those who had truly had drought damage even though we had more than 100 percent rainfall in most of the wheat area at that time. This brings us to this year's purpose for being here is to suggest that the similar drought-related damage be included in a 1989 farm legislative drought bill. We have already had damage in Texas that is worse than last year's at this same time.

In fact, the Agricultural Statistics Service reported just as late as March 19, 4 days ago, that the Texas crop is 46 percent of normal, as compared to 65 percent on this same date 1 year ago. In fact, they broke the condition of the crop down as 1 percent excellent, 8 percent good, 50 percent fair, 38 percent poor, and 3 percent very poor. We have statements attached which have been obtained from Texas Extension agronomists and entomologists that indicates that disease, insects and freeze were all enhanced in their damage due to the drought conditions.

In fact, the rainfall in the Texas Panhandle 50-year average, as the Congressman pointed out, is nearly 4 inches during the wheat-growing period between October and February. This year it has been slightly over 1 inch. And attached to your supplemental material is a graph showing that very vividly, the rainfall conditions during this important period for wheat to develop if it is to materialize and make a crop.

So this is to request that the committee, as you have indicated you are already doing, consider extending provisions of the 1988 drought into new legislation for the 1989 drought.

I would like to read one small paragraph from the Extension comments. And Texas being as large as you know that it is, we talk about the High Plains, rolling plains, low plains and Panhandle, that sort of thing. This comment is made about the Panhandle situation by the Extension Service that indicates, I think, very vividly the conditions over much of the State.

It says:

> Adequate surface moisture was available at planting time. Prolonged warm weather through January promoted greater than normal vegetation during the fall and early winter, so that available moisture was rapidly exhausted. Moisture has been so short here that cattle had to be removed from dryland wheat by early January when the normal livestock removal date is March 1. Fall and winter greenbug and mite pressure have been very high due to warm weather and droughty conditions. The exact amount of winter-kill of wheat has not yet been determined yet, but it is considered to be extensive. Winter-kill is much greater in dryland wheat, particularly wheat that had heavy, greenbug population. The extremely dry conditions coupled with the freeze and insect activity has substantially reduced potential yield of Panhandle wheat due to the drought.

While I am calling attention to the drought situation, I would like to direct another comment. It is more of a disclaimer, and, that is, that Texas produces only about 2 percent of the national wheat crop. I would like to remind the committee that at this time we have 534 million bushels of wheat projected to be in carryover stocks come June 1, and we will at that time already be 30 days into the new harvest started in Texas. And which we have not yet had a USDA crop report and will not until May, but the International Wheat Council that monitors world stocks and world conditions has already projected the United States will have over a 2 million bushel crop this year, even with the conditions that they have taken into consideration.

If that is the case, and with the projected domestic and international use during the coming year, we will add 100 million bushels to our carryover stocks a year from this June to the year 1990. So I would not want to alarm the consumers of the world that consume our wheat of any shortage of wheat. I think this is reflected in the fact that the farmers' own reserve, that farmers had thought now be triggered for this harvest due to price reaching the magic level of slightly above $4, has not reached that. This indicates to me that the grain trade, that the millers and that the bakers are not worried about a shortage either, and that their price has not been bid up to take care of their needs.

So apparently there is not any real concern of running out of wheat. Our concern here is for help to individual producers who may have had similar losses last year.

[The prepared statement of Mr. Nelson appears at the conclusion of the hearing.]

Mr. GLICKMAN. I thank you both for your testimony. It is interesting, Mr. Nelson, that in watching the daily market price for wheat, even though there has been a fairly healthy upward trend in the last 4 months, that at least as of the current time, there does not seem to be any crises or panic in terms of the market price of wheat. In fact, yesterday it was down, and I think the day before it was down as well.

There has been some strength in the soybean markets lately, but not so much in the wheat market, which indicates that in terms of world supply and demand, at least as of the present time the marketplace does not see, as you say, any particular crises.

However, I do believe that if we were to suffer a widespread drought throughout the Central Plains, that by the end of this summer that opinion would change because we still are pretty low in terms of carryovers, and I think the market is projecting a reasonable production this year. It may not happen and we are in potential trouble in terms of the ability, for example, to export anything. I do not think we are in trouble domestically at all.

Mr. NELSON. This was our concern. We thought that if, you know, look at as of today, if it continues to worsen why then make policy decisions and let legislation rest on that. We have been concerned there might be administrative decisions made against the use of EEP, their announcement programs based on two earlier considerations. And I do not think that that is really true, based on the fact that one national network had a drought story this week. I have copies of the headlines and newspapers here that say, "Drought is not to go away during this week prices of wheat have gone down." This does not indicate to me that the millers and bakers are really worried or they would be out here buying this wheat and get the price up. Or it would trigger the farmer on reserve and place a strain on the market that would then put it on its true value.

Mr. GLICKMAN. Mr. Rivinius, I guess you and Mr. Nelson both agree that Congress should consider extending the Disaster Assistance Program for 1989; is that correct?

Mr. RIVINIUS. Yes.

Mr. GLICKMAN. Do you agree with that Mr. Nelson?

Mr. NELSON. Yes. That is the main purpose I am here, to establish that position.

Mr. GLICKMAN. Is that a position of the wheat growers nationally, as far as you are aware of?

Mr. NELSON. They have not voted that as a policy, but we have been meeting with wheat growers and individually there have been concerns expressed to that extent this week.

Mr. Schwensen, our national executive director is here. May I yield to him to make a comment to you in the audience?

Mr. GLICKMAN. I see him back there. Have you all taken a position yet? You have not. I assume you would be favorably disposed toward extending it, if the problems continue? That is why we are going to have the hearing in another couple of weeks to get a better view of this. As I have said before, it would be my inclination to recommend to the chairman of the full committee that if, in fact, conditions stay the same or get worse in the next couple of weeks when we get back, then we have got to proceed with doing just that. If we have an amazing amount of moisture the next couple of weeks, and I think that it may not be as relevant, but we will just have to wait and see.

Mr. NELSON. I would like to comment, Mr. Chairman, also that it is not unusual that the Texas wheat producers may be talking about a policy change before national—and that Texas further south—we are a large wheat State. We are a large program participant State. And then what happens to us happens first.

Mr. **Glickman**. I thought you were going to tell me that Texas is such a repository of wisdom that you were always first in everything.

Mr. **Nelson**. We would like to believe that, but it is because our harvest does start in April. That is just a few weeks away in the extreme southern part of the State, so this makes these problems more eminent and the same with ASCS problems, they hear from us, I think, before some of the others, and that we hit the problem first.

Mr. **Glickman**. Mr. Rivinius, you all were hit very dramatically with the drought last year. You would really have a double whammy if it hit you 2 years in a row?

Mr. **Rivinius**. Right, and our bins are empty and again I want to concur with him. Nationwide we do not have this shortage, but in my area the bins are empty, and if we have a zero again, those farmers in that area are going to be really hurt because they will not have anything to sell, and like I mentioned earlier, that crop insurance does not cover the cost of production. And it was supposed to be doing that, but in the interim I think you will need to come up with some kind of disaster payment to cover the cost that the crop insurance will not cover.

Mr. **Glickman**. I sure appreciate your testimony and coming down here today. Mr. Stangeland.

Mr. **Stangeland**. Thank you, Mr. Chairman. I do not have a specific question except to thank the witnesses for their testimony and to tell Mr. Rivinius coming from northwest Minnesota, things look pretty favorable right now with the snow cover we have, and we are going to see some spring flooding. But unless we get spring and summer rains, we will have a flood in the spring and could have a drought in the summer, we recognize that.

I think you referred somewhat to crop insurance, and you are no doubt aware that there is a commission studying the question of crop insurance. Some of us on this committee very much want to do some revamping to crop insurance to make it more attractive to producers to buy and protect themselves and make it more sensitive to some of our particular needs up there which today I do not think it is that sensitive.

And then Mr. Nelson I want to commend you, as well, on your cautioning the consumers and the world trade that while we have got problems, as of now, unless it gets worse, we are going to have enough wheat, so we do not get any kind of a scare thing going. But obviously, and then I am sure the chairman of the full committee and the chairman of this subcommittee, and those of us who are members, recognize that we have got a potential for drought in parts of the Dakotas on down through Kansas, Oklahoma, and Texas. And that it would certainly be appropriate that we stand ready to do what we have to do to make sure that the farmers do not suffer too through this.

I am wondering how much some of your farmers are looking at 0-92 in light of the possibility and can 0-92 be made applicable to particularly wheat that is planted in the Winter Wheat Belt that now appears in some cases possibly to be virtually totally destroyed?

Mr. **Nelson**. Of course, 0-92 does not offer the attractiveness this year that it might have in the past. You only get the differential payment and with prices where they have been in the range of these last several weeks, if they should stay in that range or increase higher due to the drought, there would be no deficiency payments, and so there would be a zero income, as well as laying out and tilling your crop. And we have the additional problem in caring for the land, so we would have to by April 1, notify us if we are going to be in 0-92. You can make your mind up later, but you have to notify your intention by then. And we do not know those answers yet.

Mr. **Stangeland**. Thank you very much.

Mr. **Glickman**. Thank you very much. Mr. Volkmer.

Mr. **Volkmer**. I am sorry I was not here for your testimony, Mr. Rivinius. I would like for you to clarify my memory in regard to last year in North Dakota. Was your Winter wheat crop that you had up there bad or good last year? You do not have any Winter wheat?

Mr. **Rivinius**. We have some Winter wheat in the Southwest, but there was very little of it that was any good. Basically because the mosaic came in because of the dry conditions.

Mr. **Volkmer**. I remember all your Spring wheat, your oats, barley, everything was gone.

Mr. **Rivinius**. Right.

Mr. **Volkmer**. What you are looking at is basically the same conditions that some of my producers in the northern part of my district are looking at, even though it is not just wheat. We have Winter wheat, but we also raise a lot of beans, corn, and milo and some oats. But we are looking at the same thing that you are in Texas.

Glenn English tells me that in the Panhandle of Oklahoma they are looking at possible disasters, the gentlemen and our chairman, and Mr. Roberts from Kansas, tells us we are looking at it in Kansas. And even though it may not be nationwide, as bad as it was last year, for each one of those individual farmers, it is just as bad; is that correct?

Mr. **Nelson**. That is our concern.

Mr. **Rivinius**. And, in fact this year would be worse. Last year a lot of the farmers had some grain in the bins.

Mr. **Volkmer**. Some left over that they could use to sell?

Mr. **Rivinius**. Yes, they could take advantage of the higher market. They did that last year, and now, like I said, the bin is empty.

Mr. **Volkmer**. I will be glad personally to work with you because in a way, let us put it this way, I am thankful for your testimony because you helped the cause of my producers who I think are looking at, a number of them, a strip to the northern part of my district, are looking at another disaster, while the rest of the State is doing very well.

And if I was just going up here by myself or maybe my colleague to the west from Missouri and just a couple of us complaining, we might not get anything done, but with enough people we might get something done for next year. And the gentleman from Minnesota, I want you to make sure the next time we talk about all the States you include northern Missouri. And I think after we listen to Iowa, we may find that southern Iowa may be pretty much in that shape too.

So we do have areas in parts of western Illinois the same way. So I think it is going to be imperative for us to do as the chairman says, in a couple weeks we will look at it and make a decision of what we are going to do in the future. I appreciate your testimony here today.

Mr. GLICKMAN. Thank you, Mr. Volkmer. Mr. Sarpalius.

Mr. SARPALIUS. Mr. Chairman, I really do not have much more to say. We pretty well covered everything, but I want again to thank the individuals here for coming today and expressing their views on the problems we are having with wheat crops. And a little bit more on that, as Mr. Nelson explained, up in our area we produce a lot of feed lot cattle, and we basically took away any opportunities there for grazing those cattle on Winter wheat this year. There just was not enough wheat there to graze. So it not only had an impact on the wheat crops, as well, but it has had some impact on the farmers out there who have been accustomed to utilizing that grazing for their cattle, as well. I appreciate your coming today.

Mr. GLICKMAN. We thank you all very much for testifying. You have been most helpful. Our last set of witnesses is a panel and I know you all have been waiting a long time and I apologize for that, but at least a couple of you have been around here many times before, maybe all of you have.

We have Don Gingerich, president, National Pork Producers Council. We have Chandler Keys with National Cattlemen's. Steve Kopperud with American Feed Industry Association. We appreciate your all being here. Your statements will appear in the record in their entirety if you summarize, so if you want to summarize, that is fine with me as well. Chandler, you begin, then we will go to Steve, and then we will go to Don. So, Chandler, please begin.

STATEMENT OF G. CHANDLER KEYS III, DIRECTOR, CONGRESSIONAL RELATIONS, NATIONAL CATTLEMEN'S ASSOCIATION

Mr. KEYS. Mr. Chairman, thank you for allowing the National Cattlemen's Association to testify here today. We feel we have some pertinent points to bring up.

As you know some time ago, the room was really full, a lot of people and tempers were flaring and we put together a pretty good bill we thought. The National Cattlemen's Association thought that the bill, at the time of passage worked out real well and took care of a lot of our concerns.

We also know the livestock industry needed to be taken care of immediately because the effects of the drought are felt first on the animals that are grazing, using the water holes that are drying up, all over the drought areas.

So we want to take this time to say at the beginning of the drought, we feel the USDA did an admirable job on instituting programs and projects that alleviated the burden of the drought on the livestock industry. It allowed haying and grazing. It allowed haying on the CRP, implemented the existing feed programs and probably more important than anything, they purchased red meat early on to ease market pressure from added cow slaughter. NCA at this time felt it was very advantageous to do so because excessive slaughter would have been a disaster in light that the United States has the smallest cow herd in almost 40 years.

We also know the disaster bill was developed to give USDA added statutory authority to develop and further help American farmers and ranchers. And the act basically had two provisions, one for crops and one for livestock. And we are very thankful again to the Congress for putting together this program.

At this point we feel that there were no major catastrophes in implementing the bill, even though for our purposes today, I would be remiss if I did not elaborate on USDA's problems, misunderstandings, general foul ups and disregard for the intent of Congress while propagating the regulations for the emergency feed programs.

First of all, Mr. Chairman, it took almost 2 months for the USDA to finally put together the emergency livestock feeding interim regs, but only took about 1 month to do the crop disaster program regulations. But the enactment date was August 26, so that meant that the local ASCS offices were in the dark and confused on what type of programs to use when they were trying to fill out applications and getting the help to our ranchers and farmers.

So we have got a few things I would like to hit real briefly on that we felt that could have been a better job or could have been implemented.

First of all, the water problems. One of the biggest things with our ranchers is not so much they have got some feed on hand. Sure they can feed cattle, but when their water supplies are all running out, they needed a program. Well, there is a program. It is called the Emergency Conservation Program. It has been a program that has been in place for a long time. But we knew when we were writing the bill that we needed to do something more, so we put another emergency livestock water program in the bill, but the USDA did not implement this citing that the Emergency Conservation Program is in place.

To apply for this Emergency Conservation Program, you have to go in before you do any of your water projects to get the approval for cost-sharing. A lot of the producers did not even know about the Emergency Conservation Program and went ahead and constructed. Of course, they were forced to put together their water projects and then they found out about the ECP, and went into the ASCS office and they say sorry guys, we cannot help you out because you should have come in before you laid that PCV pipe or dug that water out of a dried up streambed. NCA went to the USDA and tried to see if it could do some type of reimbursement program on the Emergency Conservation Program; they denied it.

Another problem is the livestock transportation. I will be real brief with this. Basically we had some producers in eastern Montana and North and South Dakota, hard hit areas of the drought that trucked some of their core cow herds down into Nebraska and Kansas where the drought was not as nasty. And we feel that the USDA could have implemented this transportation assistance program with very little cost, but would have helped a lot of the producers that took this drastic measure to try to save some of their cow herds.

I would like to elaborate a little bit more on what Congressman Smith went into today on the income restrictions. We understand the political forces that basically started this income restrictions, but we feel that there are two areas that need to be adjusted.

First of all, we feel the cost of purchased livestock should be subtracted from the gross income before applying the $2.5 million test. A farmer feeder who buys, let us say, a bunch of steers at 600 or 700 pounds, pays so much money for them and then sells them now at 1,000 to 1,100 pounds, he is only realizing money on the added value of that calf, not on the whole value because he had to purchase this calf at 700 pounds. So NCA thought that maybe if it could work on some legislation, we could work that problem.

Second, many farmer feeders, especially in California and the West Coast, went into the program early using the old program, again Representative Smith alluded to this earlier, and Congress definitely put a section in the bill that would grandfather them in under any circumstances. And because they were over the $2.5 million, August 26, they stopped receiving payments, even though they had basically planned out their marketing program in a whole-year basis. This feed assistance was needed because of the dry weather in their areas. They were immediately cut off at that point in time.

There is now talk about a group of California cattlemen going to court and suing over this problem using the provision. We did do extensive correspondence with the USDA on this issue and they ruled against us.

The animal unit. This is really a stickler for us too. We cannot understand why the USDA has not gone back and refigured the animal-unit, they use the animal unit figure that they developed in the 1940's when beef cows were probably only 900 to 800 pounds. Now we have got the average beef cows over 1,100 pounds. We feel that they need to go in and revamp that unit to adjust for the larger beef cattle. They have done it for the dairy industry. They have moved their units up to 2 from 1.5, and we have asked them to go back and do that for beef cattle.

CRP acres. We formally partitioned USDA to open up acres for grazing in drought areas. They declined citing major opposition from environmental groups. Environmentalists feared overgrazing and wildlife destruction, even though the haying of these acres had been allowed for months before.

It just bewilders NCA how a cow can be perceived as more destructive to a field of grass than an indiscriminate hay mower. We doubt that many farmers can cite an incident of a cow stepping on a pheasant or some quail, but we are sure many can attest the hay machine cutting through a nest of birds. We hope USDA will not discriminate against grazing in the future based on such frivolous arguments.

Other problems we attest to today include the crop insurance, but now it is being taken care of. But I cannot understand why it was not taken care of at the beginning. Now farmers and ranchers are going to have to go back in, many of them, Mr. Chairman, went ahead, forgot about the livestock feeding programs, used their crop acres in the crop disaster, received less money, and still had to feed the livestock that they had on hand. They are not going to be able to go back now, now that the crop insurance provision is being taken care of, because they have already been receiving payments on the crop disaster.

Also I had a call from a NCA member who is denied eligibility in Illinois because the cut-off date for requesting pasture loss in Illinois evidently was November 1988. But they told him in November that he could not apply for disaster payments because he still had feed on hand; come back in January. So when his feed ran out in January, he went back in, he said sorry, we cannot help you because the cut-off date for pasture loss documentation was November. He was just furious.

In closing, NCA believes the Drought Assistance Act of 1988 was a good effort by Congress. It helped alleviate some of the financial hard times facing farmers and ranchers. And for the most part USDA, especially early on, used their resources effectively.

However, we know a much better job could have been done in implementing the livestock assistance programs. Some of the blame must be laid at the feet of OMB, but USDA, we believe, did not fight hard enough for the people they serve when dealing with OMB.

Another point, ASCS must deter from the mind set that every farmer/rancher in this country is a crook or a cheat. This only breeds resentment and lack of faith between Washington and the country.

For all the good intentions in the drought bill, Mr. Chairman, it may be for naught with many livestock producers because of a lack of good follow-through and good faith on the part of the USDA in the end. Thank you.

[The prepared statement of Mr. Keys appears at the conclusion of the hearing.]

Mr. VOLKMER [acting chairman]. Thank you very much. We are going to hear from Mr. Kopperud.

STATEMENT OF STEVE KOPPERUD, VICE PRESIDENT FOR LEGISLATION, AMERICAN FEED INDUSTRY ASSOCIATION

Mr. KOPPERUD. Thank you, Mr. Chairman. At the outset, AFIA, the American Feed Industry Association, would like to associate itself with the remarks of the cattlemen and pork producers.

AFIA's involvement in feed assistance programs goes back to 1949 when Congress included in the Ag Act of 1949 the feed dealer option which allowed the Secretary to use the realworld infrastructure in the feed industry to advance immediate feed assistance. We were gratified to see Congress and this committee and particularly this subcommittee move as quickly as they did last summer on drought action. And we commend the subcommittee for this review.

We too ran into our problems with the USDA. I think it is apparent to all of us that what we did on the Feed Assistance Act was not necessarily as complex a change as may have been perceived. We broadened the number of eligible producers. We broadened the number of eligible counties. We brought some ancillary aspects into it, but the delivery mechanism for feed assistance was essentially the same as was created in 1977 and modified slightly in 1985.

So our frustration over why it took, as Chandler mentioned, more than 2 months for the Department to come up with the rules for implementing the program and despite the fact that 10 national agricultural organizations wrote to the Secretary urging a speedy implementation of the act, it still was not until October 14, almost 2 months after the effective date of the assistance, that we saw the interim rule. We still have not seen a final rule. We understand that the final rule is at OGC. And hopefully we will see it soon.

Where we found our major problem is that one change that Congress did make and first made on the House Agriculture Committee was to expand the definition of eligible feed products for cost-sharing, and they expanded it by including premixes. Premixes were integral to a lot of on-farm mixers, a lot of smaller producers who did not routinely buy complete feeds, for whatever reason, their personal preference, their investment, whatever.

There was report language in the House passed bill and then finally the bill that President Reagan signed that said, under no circumstances does Congress intend to force a producer to shift his feeding practices based on the type of assistance available. Well, what we ran into was a whole different situation. AFIA started receiving calls almost immediately that not Washington, and in most cases not State ASCS, but county ASCS offices were refusing to implement at least the premix definition, and, in general, most of the changes that Congress had made in the Disaster Assistance Act of 1988.

And we started meeting with ASCS about it. And I know that Mr. Newcomb was as frustrated as we were about why some very clear, concise instructions to the county ASCS offices were not being met. We ran into the situation mainly in Ohio, Indiana, Illinois, Wisconsin, and Minnesota. And we can only surmise that the reason those States had the most difficulty was it is those States which have not traditionally had to implement disaster feed assistance programs due to drought and natural disaster.

Mr. Newcomb has tried hard to get these things worked out but we are still today—yesterday I got a call from a farmer in Bedford, Virginia, wanting to know why his neighbors in North Carolina could get feed cost-sharing on premixes and his neighbors in West Virginia could get cost-sharing on premixes, but for some reason his county ASCS office decided not to allow cost-sharing on premixes.

The day before we had gotten a call from two different companies in Wisconsin, saying that a premix product had been disallowed for cost-sharing because the carrier, the binding agent in the premix was yeast. And yeast by ASCS definition in Wisconsin, at least, for whatever reason, is considered inedible by animals when it has been a feed ingredient for about 50 years.

So these are our frustrations. We are curious as to why the Department has moved so slowly. I agree with Chandler, we know that there were problems with OMB early on and we would concur that we wished USDA had fought back a little harder when OMB was pulling some strings.

One of the frustrations a lot of our companies are facing right now includes the effective date. Because the effective date of the assistance was August 26, but applications were not accepted until October 1, it was our understanding in the communication to our members that farmers would receive retroactive assistance back to the effective date, despite the date of the acceptance of their application.

But across the mid-West that was not the case. Farmers were coming in on October 1 seeking application. In many cases the counties were saying, we have not got the final rules. We do not even have interim rules. We are not going to accept applications until we get them.

When they finally went back in, they were told their assistance would begin on the date of application and forward, not back to the August 26, congressionally intended effective date. A major problem for a lot of producers. It creates a lot of customer relations with the feed companies who are trying to forward the stuff as fast as we can to the people who need it.

Again, I am not complaining as much about ASCS Washington as I am about the State and county infrastructure out there. It seems to have broken down on this program. It seems to have broken down on a regional basis, primarily the Central Midwestern States seem to be having the primary problem. As I said, I know Mr. Newcomb has tried very very hard to get these things straightened out, but unfortunately it has not worked to the degree that we expected it to.

We also have a problem with the formulation on cost-sharing. As you know, cost-sharing can go one or two ways. They can either do a straight 50 percent of the cost as invoice to the producer or they can do it on a cents per pound per basis to the producer. It seems to us to cost-share on a complete feed at a straight 50 percent of the cost makes sense. But to then take and penalize the on-farm mixer by cost-sharing on perhaps 50 percent on the grain he buys, then a cents-per-pound formula on the premix and whatever other ingredient, simply is not fair. The reason it is not fair is that when the formulation is worked out, that on-farm mixer is getting less cost-sharing than he would if he bought the complete feed.

Again it goes back to the point we were not trying to force farmers out of traditional feeding practices or mixing practices into another feed product. We were hoping to be able by including premixes to maintain that balance, both on the producers and on the feed companies.

I will end my statement there and wait for questions. As I say, it is not ASCS Washington that we have had a problem with. We commend the committee for the action they took. But we have got to work out some kind of a more concise or at least a more direct communication system in county ASCS offices.

[The prepared statement of Mr. Kopperud appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much. Mr. Gingerich.

STATEMENT OF DON GINGERICH, PRESIDENT, NATIONAL PORK PRODUCERS COUNCIL

Mr. GINGERICH. Thank you, Mr. Chairman and members of the committee. I am pleased that you had this hearing today and that I have this opportunity to testify on the Disaster Assistance Act of 1988. I personally want to thank you as a committee for the support of the National Pork Producers Council and the things that you have done for us over the years, and especially for the legislation which you created during the month of July 1988. That was expedient to say the least.

I am representing the 100,000 pork producers across the Nation here today, and feel as though they had a big interest at stake as this legislation was passed and then also attempted to be implemented. I have a written testimony for the record. I will submit it, but will abbreviate to some extent and touch on some of the most important parts.

Mr. VOLKMER. All of the prepared statements will be made a part of the record. So you may summarize if you wish.

Mr. GINGERICH. We do believe one important point that the committee needs to know how effective the drought relief legislation was in helping producers in this serious time of need that we had. Now the relief provided through the U.S. Department of Agriculture has been less then acceptable to pork producers. They were either deemed ineligible for feed assistance programs or if they were eligible, the level of assistance provided was usually negligible.

As of February 28, only $243 million in emergency feed benefits had been distributed to all livestock producers, including beef, dairy, lamb, and pork producers. These outlays were far short of the original estimate and the intent of Congress on that, I am sure.

It is obvious that the emergency feed programs are not designed to reimburse livestock producers for their actual losses. Crop assistance payments, in contrast, are designed to reimburse crop producers financial loss when possible. Livestock producers only receive feed assistance to provide a survival ration of feed to keep their animals alive.

Under the crop disaster assistance, crop producers have received $2½ billion as of February 28. This discrepancy treats livestock producers at a much lower level. Part of the problem with the emergency feed programs is that the livestock rations reflect conditions in agriculture, some 40 years ago. These rations are outdated and are not suitable for today.

For instance, for a full grown sow, pork producers are allocated a survival sustenance ration of 3.3 pounds of feed per day. For swine less than 6 months old, the eligible pork producer looks forward to a ration of 2 pounds of feed per day, and producers of other species, particularly cattle, have rations that are also similar under the requirements for the daily consumption.

We as pork producers believe that the feed ration is extremely low and in some cases possibly inhuman to animals. We ask that the committee work to ensure that livestock producers obtain a fair ration for their feed.

Because 20 to 25 percent of our producer members do not grow their own feed, we requested that they also be eligible for feed assistance under the new drought legislation. Many of these producers that do not graze their own feed are being penalized for making the best use of their resources. We have members with limited opportunities to grow their own grain because they are on hilly land. Others are struggling to make a start and do not own large acreage of cropland. It is hard to comprehend how providing assistance to these producers could cost $2 billion as estimated by OMB. The whole program for all other livestock producers amounted to the outlay of less than $300 million.

It appears that ASCS has interpreted the emergency feed programs so narrowly, that only a few pork producers are eligible. Although section 1763(a) of the 1985 farm bill, and report language included in the Disaster Assistance Act of 1988, specifically states that feed must be suitable for the particular animal. ASCS continues to interpret the law in such a fashion to use surplus hay or pasture as a reason to deny pork producers access to the benefits they deserve.

And once again that example you used earlier about the producer with 3,000 pigs and two 4-H cows is denied eligibility. I really agree with you that it would take less than 10 minutes additional calculations to make the difference whether a farmer might stay in business or not. Put in that perspective it is well worthwhile. And we want to work with the Washington office, and not against them as they try to develop a program that would do that.

Limitations on cost-sharing for well constructions have also surprised many of our members. Producers who were forced to dig new wells when the drought dried up their supply of water for livestock have also discovered to their dismay that they are not generally eligible for cost-share reimbursement under section 607(b)(2) of the Emergency Livestock Act of 1988. Reimbursement of costs in construction or deepening of wells for livestock water should not be limited to grazing situations only. Pork producers who demonstrate legitimate need should be eligible for this type of cost-share assistance.

We understand from ASCS that pork producers will have their eligibility for feed assistance for the current feeding year extended to the fall of 1989 when the next crop is available. Because hogs consume grain throughout the year and cannot make use of pasture in the spring, and I guess I agree with you, Congressman Volkmer, that very very few pigs live on pasture these days. They should be clearly eligible for feed assistance throughout the fall of this year.

But because we are concerned about the multispecies situation where the farmer has a mix of hogs and cattle, we understand that ASCS will deny access to the feed programs through the fall of 1989 fall crop harvest, where the farmer has access to hay or pasture, if he has a few cattle. I can speak from personal experience that my hogs, once again, do not live on pasture.

Let me say again, that the committee should be commended for its immediate action to farmers during the drought of 1988. Last year was certainly a tough time and all farmers need to understand the grave difficulties in striking a balance between various interests. We commend you as a committee for that effort.

It is unfortunate that the livestock programs division of ASCS continues to be unable to write or enact the final rules of the emergency feed regulations. Although the legislation was passed by Congress some 7 months ago, it is also unfortunate that the final regulations are not available when the last day for application under the feed program was March 31 of this year. Of course, we can resubmit applications for feed assistance after next week, but much of the confusion over the program at the local level could have been avoided if the livestock division had been more diligent in getting the rule out. We do understand that a new handbook is coming out to assist with the emergency programs.

We realize that the Secretary of Agriculture has an extremely hectic schedule, but we believe that he needs to have at least one of his representatives go to the country and visit firsthand with local ASCS offices and livestock producers. After walking through the procedure to apply for feed assistance, it would be immediately obvious that the regulations and attendant paperwork are unduly confusing and also unreasonable.

We ask that you investigate the livestock division's apparent lack of responsiveness and assess whether an extension of time for producers to apply for the Emergency Feed Program would be appropriate under the circumstances. We would also like to see an accounting of benefits distributed to livestock producers in 1988 and 1989. Quite frankly, I am concerned that producers have been unfairly turned away from potential feed benefits for reasons not intended by Congress.

An example of my county. I am in Iowa County, Iowa, and there are 1,900 checks written for crop assistance in a county where almost everyone raises livestock. There were 1,900 for crop assistance and only 75 checks written for livestock feed assistance, and only a handful of them were pork producers. The National Pork Producers Council offers its service to sort through the complexities of the feed assistance program. We can look forward to working with this committee on issues as they arise. Thank you.

[The prepared statement of Mr. Gingerich appears at the conclusion of the hearing.]

Mr. VOLKMER. Thank you very much. The gentleman from Minnesota, Mr. Stangeland.

Mr. STANGELAND. Thank you, Mr. Chairman. I would like to commend all of you for some excellent testimony. I really have no questions. I have a couple comments, but as the chairman said in opening the hearing we recognized we did not write a perfect bill. I do not know if we could ever write a perfect bill, but your constructive criticism of the program, I think, gives us a real good road map, should the need ever arise to write another one.

You have had firsthand experience with some of the glitches or blitzes and the problems, both in the legislation and in the regulations that implement that legislation. It will be made a part of the permanent record, and I am sure that this committee, if required in some future time will, look at this and take it into account, and we can do a better job in writing a law.

Mr. Gingerich, I was the author of the bill that would have provided feed assistance to those producers who did not grow their own feed. Because of the budgetary considerations it was defeated in this committee. And I think properly so, I am not sure. I was concerned in my area with a lot of turkey growers, a lot of dairy farmers, and I am sure pork producers in other parts of the country. I do not know if the figure of $2 billion is a correct one or not. I do not know how you access that.

But let me assure the cost would have been substantial. But I believe that those farmers were being impacted by higher feed costs just as severely as those people who grew their own feed. And then, Mr. Keys on your critique and criticisms I can agree with a good share of them. I am just going to give you my perspective on grazing on CRP and maybe it will help NCA, if you will take it back to them as to why some of that was done.

I happen to be a farmer and I happen to run cattle when I was actively farming before I became a Congressman. And it was my belief that some of the CRP had gotten quite rank and course, when you hay that you can get the cows to eat it. When you run them on it, they trample 80 percent of it. If the growth, and I think the opposition of the wildlife people is overplayed, if you have a sparse growth and it is not worth haying, chances are you are going to herd cows over there on extremely dry conditions. You are going to chew up that ground and subject it to erosion and they are probably not going to get that much feed benefit out of it. I think you might want to look at that critique and think that it is probably not as germane as it should be.

Plus when you do mow and I can recognize it, I caught heck from wildlife people because we mowed and could have destroyed nests, but when you do mow you leave a little stubble and I think what our main concern was the future of that land as far as its ability to reproduce and not damage or totally destroy what vegetation was there in that drought year and also to better utilize whatever the land produced, and you better utilized that by putting in a bail. And if it was course, you could put more acids or some tasty additive to get the cows to eat it, whereas you run them out there and you graze them and they destroy substantially more than they would ever gain from it. I just really think that one—but your other points are pretty well taken, as are yours, Mr. Kopperud.

I want to commend you for coming in here and very rationally, first of all commending us for what we did, and then tell us what we did not do. I think that it is appropriate. Thank you very much.

Mr. VOLKMER. Thank you. Mr. Keys, we have had quite a bit of a water problem in northeast Missouri. The conservation program that you mentioned provides for basically digging of wells, drilling of the wells, 50 percent cost-share. In that area where our drought is occurring, you are just wasting money drilling wells because you might get 3 gallons a day, if you did it, and then it is going to be rusty and sour and salty and everything else.

And we were able to persuade ASCS and they did look at the situation and realize that farmers up there provided a water source from standing water ponds and lakes. And they have come along with a cost-sharing to provide for pumping from streams and from larger conservation lakes or other lakes that have water supply to farm ponds.

But we still do not get that water for anything but out there in the pasture.

Now that goes back to the different livestock. We have people that have hogs. They have hogs basically in confinement. They did not get any water. They cannot get any water. And the people that have kept their livestock off the pasture because the pasture is too dry and wanted to bring water in through tanks and such could not get any assistance, they had to pay for it themselves.

Plus the people who pumped early, that goes back to what you said, the people who pumped, some back in December and early January before we got them to agree to do it, they did not get reimbursed. And to me we tried the same thing, we got nowhere with them. So we would be glad to—because in my opinion, from what I have heard here, I am going to do everything I can to rewrite parts of the livestock assistance program that was in that drought bill and the permanent law. That is permanent law, so we have to do that, if we are going to effect what is going to happen this coming year. Because in my opinion we are going to have some drought in parts of this country where it is going to be applicable in this coming year.

I would be glad to work with you on it and the same way with Mr. Gingerich, with you all, also. Because I guess all of you heard my little temper with the ASCS people over the use of hay for hogs. Now maybe I am wrong, Mr. Von Garlem says that some places they still pasture hogs. Now, they may be, but I would question the food value of that hay in producing hogs and getting hogs up as fast as you can good quality meat; would you not say that Mr. Gingerich?

Mr. **Gingerich**. That is right. I think if you see hogs on pasture, you will see them for the purpose of a good clean place for them to be rather than a source of food for them.

Mr. **Volkmer**. Usually when we have them out, we see fewer and fewer, but what we call a hog lot is part of a field that is fenced off and hogs are out there, and like I said in my other testimony this morning, within a year there was not any grass or anything else there, but everything out there. We had feeders out there that the hogs ate their rations from in that lot. Is not that what usually happens, they are not just living off of that grass?

Mr. **Gingerich**. That is exactly right. They usually are very hard on grass and the grass dies if you keep them there very long, so pasture is not a source of feed for very many pigs in this country.

Mr. **Volkmer**. I would like to work with you. I thought that I had written it back in 1985 clear and I did not do it. This was first brought to my attention, by the way, back in 1983 when we had a drought in our district and some of our pork producers also have livestock and they are very diversified and raise a lot of their own grain. They also have some pasture and raise some hay. They are finding out that they were not going to get any assistance at all because they had so much hay, et cetera, on hand.

So somewhere along the line I want to rewrite that so that it says what I think it says. And that the feed has to be suitable, the same nutrition value, in other words, for the respective livestock. If you could help me on that I would appreciate it.

To be honest with you, last year when I thought about this, I talked to one of my farmers and I thought about going ahead and bringing a class action suit myself because I have been very frustrated by ASCS and their actions. I think it was very clear from the discussions here when we had the amendment, especially last year. It should have been very clear to them what was intended with that language, and yet I found out last fall that they still were not doing it that way. And I found out today by calling one of my local offices that they still are not doing it that way. I heard today from the ASCS hearing testimony that they were not doing it that way.

I know of no other way of doing it, other than to write the language, even if we write, unless they provide me with the language that I ask for, I still do not know what they are going to do. So maybe it is going to be necessary to bring a class action suit. I think the intent of Congress will be very clear from what we had in the record here on it.

With that, I think what is going on, what testimony we also have heard from the gentlemen from the previous panel from North Dakota and Texas and my discussions with, like I said, with other people from other States, that we are going to maybe not have as bad a drought so far. But it looks like we are going to have some drought in this country. Iowa is looking a little better; right?

Mr. GINGERICH. We are extremely dry in our area. The drought persisted throughout the winter, no snow or rain.

Mr. VOLKMER. Pardon?

Mr. GINGERICH. We had very little snow or rain this winter.

Mr. VOLKMER. I know southern Iowa is still bad and the northern part of my district, the southeast especially is still pretty hard hit.

Mr. GINGERICH. That is correct.

Mr. VOLKMER. We are getting to the point where what rains we get this spring really are not going to help it that much because at the subsurface, we do not have any moisture.

With that I want to conclude the hearing, I thank you very much for your testimony and look forward to working with you. I would like, Mr. Keys, to especially work with you on the water problem to see if we cannot straighten that out. Also, to make it very clear what is included.

Mr. KEYS. Just one point on that. The most important thing to a lot of our producers, if they are going to ask the Government for any help, they would like it in the form of water help, not so much feed, but water is the most important thing.

Mr. VOLKMER. That is true in what I say. A lot of my farmers have gone through a lot to keep them from going to the market. I have had farmers that have bought city water and truck tanked it out to their farm and that gets pretty expensive to haul it, but they have done that through this winter. We still have a lot of ponds that are dry, so I will be glad to work with you. Thank you very much. That will conclude the hearing.

[Whereupon, at 1:25 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

[Material submitted for inclusion in the record follows:]

Statement by Milton Hertz
Administrator, Agricultural Stabilization and Conservation Service
U.S. Department of Agriculture
before the
Committee on Agriculture
Subcommittee on Wheat, Soybeans, and Feed Grains
U.S. House of Representatives
March 23, 1989

Mr. Chairman and Members of the Subcommittee, I am glad to appear before you today to discuss the implementation of the 1988 Disaster Assistance Act and other issues related to the drought of 1988.

The Disaster Assistance Act was signed on August 11, 1988. Many of our Agricultural Stabilization and Conservation Service (ASCS) employees were already familiar with this legislation so we were ready for training meetings in September, on both State and local levels. ASCS county offices began accepting applications on October 1.

Disaster Payments

The farm program payment yield was used as the disaster payment yield on program crops for both participating and nonparticipating producers.

One of the biggest problems we have had implementing this legislation has been establishing payment yields and payment rates for nonprogram crops. The Secretary determined that we would use yields for nonprogram crops based on the National Agricultural Statistics Service (NASS) data, if a producer did not have acceptable actual production evidence. Payment rates and yields have been established for 483 nonprogram crops. We will submit a copy of this list for the record.

Payment rates for program crops for producers participating in the 1988 Programs were based upon the target prices, and for nonparticipating producers the price support loan rates were used. For soybeans and nonprogram crops, Farmers Home Administration (FmHA) data for crops that do not have a marketing year were used, and NASS data were used for crops that do have a marketing year, excluding the highest and lowest rate for the five immediately preceding years, and averaging the remaining three years.

As of February 28, 1989, over 558,000 producers have received disaster payments and emergency feed assistance amounting to over $2.7 billion.

Emergency Feed Assistance

Because of the feed losses attributable to the 1988 drought and related causes, livestock feed programs have been implemented in 2189 counties in 42 States. Since many counties had no experience in administering emergency programs, there was some confusion at first resulting in delays in serving applicants. Additional instructions, training meetings, and automated assistance have allowed ASCS to effectively administer these programs for livestock producers.

Most of the assistance to eligible producers will be channeled through the Emergency Feed Program (EFP) which provides cost share assistance for feed purchased, and the Emergency Feed Assistance Program (EFAP) which makes Commodity Credit Corporation (CCC) owned grain available for purchase at reduced prices.

Through January, a total of 121,581 applications have been approved for assistance on more than 17 billion pounds of feed needs (on a feed grain equivalent basis). Under EFP, cost-share payments of more than $240 million have already been issued to 82 thousand producers. Under EFAP, 7,000 producers have purchased 18 million bushels of feed grains from CCC priced at 75 percent of the applicable loan rate, which amounts to assistance valued at about $18 million.

Aflatoxin Contamination

Although you may be holding another hearing next month on aflatoxin, we wanted to make just a few comments today regarding the matter. There have been several reports of problems with aflatoxin in corn due to the drought. In September 1988, ASCS announced that corn contaminated with aflatoxin would not be considered as production for disaster purposes if the corn is destroyed so as to render it inaccessible to livestock or wildlife and the producer will receive no feed or financial benefit from the sale of this corn. CCC will not accept delivery of corn contaminated with aflatoxin in levels of 20 parts per billion or more in settlement of price support loans.

There has also been widespread concern that the development of aflatoxin in drought-affected feed crops harvested in 1988 may provide a public health hazard as these crops are fed to livestock, particularly to dairy herds. The departments of health of the State governments monitor the quality of milk produced for commercial markets, and some increases in aflatoxin levels were reported in certain areas. If the levels exceed the tolerances established by the Food and Drug Administration, those specific producers are notified their milk cannot be marketed, and the milk must be destroyed by dumping.

The dairy producers who are directed by a public agency to remove their milk from the market can be compensated under the Dairy Indemnity Payment Program for the market value of the milk so removed, if the contamination is determine to be inadvertent. Generally, the level of aflatoxin in milk drops very quickly when the contaminated feed is taken away, so the time a producer is off market is very brief.

Through February, 28 applications have been approved for indemnity payments totaling $114,000 due to aflatoxin contamination. Based on a survey, we estimate about 35 additional applications will be received, and therefore it appears the $579,000 available to pay eligible claims in FY 1989 will be sufficient to cover all losses due to aflatoxin.

In checking with our ASCS State offices, there doesn't seem to be as much aflatoxin as was first thought.

This concludes my statement, Mr. Chairman, and I will be happy to respond to questions.

(Attachment follows:)

1988 DISASTER PROGRAM - DASCO APPROVED CODES

CROP NAMES, ABBREVIATION CODES, NUMERIC CODES AND UNITS OF MEASURE

As of 3-16-89

Almonds	ALMND	0028	lbs
Amaranth Grain	AMAGR	0516	lbs
Apples, Crab	CRABA	0462	con
Apples, Fresh	APPFR	0368	con
Apples, Processed	APPPR	0369	con
Apricots	APRCT	0326	con
Artichokes	ARTIC	0458	lbs
Artichokes, Jerusalem	ARTIJ	0522	lbs
Asparagus, Fresh	ASPFR	0229	lbs
Asparagus, Processed	ASPPR	0230	lbs
Avocados, Fresh	AVOFR	0231	con
Avocados, Processed	AVOPR	0232	con
Babaco Papayas	BPAPY	0493	lbs
Barley	BARLY	0091	bu
Basil	BASIL	0340	bun
Beans, Baby Lima	BLIBN	0057	lbs
Beans, Black Turtle	BLTBN	0278	lbs
Beans, Butter	BUTBN	0277	lbs
Beans, Castor	CSTBN	0122	lbs
Beans, Chinese String	BODBN	0283	lbs
Beans, Cranberry	CRNBN	0279	lbs
Beans, Dark Red Kidney	DRKBN	0059	lbs
Beans, Faba	FABBN	0457	lbs
Beans, Fava	FAVBN	0282	lbs
Beans, Flat Small White	FLWBN	0063	lbs
Beans, Garbonzo	GARBN	0422	lbs
Beans, Great Northern	GRNBN	0065	lbs
Beans, Green	GREBN	0295	lbs
Beans, Jacobs Cattle	BEJCT	0696	lbs
Beans, Large Lima	LLIBN	0066	lbs
Beans, Light Red Kidney	LRKBN	0068	lbs
Beans, Lupin	LUPBN	0371	lbs
Beans, Marafat	BEMAF	0697	lbs
Beans, Miscellaneous Lima	MLIBN	0111	lbs
Beans, Mixed	MIXBN	0069	bu
Beans, Mung	MUGBN	0395	lbs
Beans, Pink	PNKBN	0115	lbs
Beans, Pinto	PINBN	0113	lbs
Beans, Small Red	SMRBN	0107	lbs
Beans, Small White	SMWBN	0109	lbs
Beans, Snap Green, Fresh	BESGF	0594	ton
Beans, Snap Green, Processed	BESGP	0595	ton
Beans, Snap Wax, Fresh	BESWF	0592	ton
Beans, Snap Wax, Processed	BESWP	0593	ton

Beans, Soldier	BESDR	0698	lbs
Beans, White Kidney	WIKBN	0281	lbs
Beans, Yardlong	YLGBN	0506	lbs
Beans, Yellow Eye	YELBN	0280	lbs
Beets, Fresh	BEEFS	0642	con
Beets, Mangel	BEEMG	0438	con
Beets, Processed	BEEPR	0643	con
Beets, Red	BEETR	0333	lbs
Beets, Red, for Feed	BEERT	0699	lbs
Birdsfoot Forage	BIFFO	0355	ton
Blackberries	BLBER	0302	con
Blackberries, Evergreen	BLBEV	0409	con
Blueberries, Fresh	BLUFR	0233	con
Blueberries, Processed	BLUPR	0234	con
Bokoy	BOKOY	0306	lbs
Boysenberries	BOYSN	0418	con
Broccoli Robb	BRCCR	0700	con
Broccoli, Fresh	BRCFR	0235	lbs
Broccoli, Processed	BRCPR	0236	lbs
Brussel Sprouts, Fresh	BRUFR	0237	lbs
Brussel Sprouts, Processed	BRUPR	0238	lbs
Buckwheat	BUKWT	0114	bu
Cabbage, Chinese	CABCH	0507	lbs
Cabbage, Fresh	CABFR	0240	lbs
Cabbage, Processed	CABPR	0241	lbs
Cai Lang	CALNG	0678	con
Cantaloupes	CANTA	0118	con
Caraway	CARWY	0539	lbs
Carob	CAROB	0494	lbs
Carrots, Fresh	CARFR	0242	lbs
Carrots, Minie	CARMI	0332	con
Carrots, Processed	CARPR	0243	lbs
Catnip	CATNP	0644	lbs
Cauliflower, Fresh	CLFFR	0244	lbs
Cauliflower, Processed	CLFPR	0245	lbs
Celeriac	CLERI	0509	con
Celery	CLERY	0126	lbs
Cherries, Fresh	CHEFR	0246	con
Cherries, Processed	CHEPR	0247	con
Cherries, Sweet	CHESW	0372	con
Cherries, Tart	CHETA	0373	con
Chestnuts	CHENT	0375	lbs
Chicory	CHICO	0511	lbs
Chives	CHIVE	0513	lbs
Chufas	CHUFS	0645	lbs
Citron	CITRO	0472	lbs
Collards	COLLD	0317	con
Coriander	CORIA	0540	lbs
Corn	CORN	0041	bu
Corn, Blue	COBLU	0596	con
Corn, Miniature Sweet	CORMS	0367	lbs
Corn, Sweet, Fresh	SWCFR	0212	con
Corn, Sweet, Processed	SWCPR	0213	ton
Cotton, ELS	ELSCN	0022	lbs

Cotton, upland	UPCN	0021	lbs
Cranberries	CRNBR	0058	bbl
Cucumbers, Fresh	CUCFR	0248	lbs
Cucumbers, Processed	CUCPR	0249	lbs
Currents	CURRN	0325	con
Dates	DATES	0496	lbs
Dill	DILL	0341	bun
Dandelions, Domesticated	DANDD	0679	con
Egg Plant	EGGPL	0318	lbs
Elderberries	ELDBR	0417	con
Endive	ENDIV	0329	lbs
Escarole	ESCRO	0330	lbs
Fennel	FENNE	0523	lbs
Figs	FIGS	0060	ton
Flax	FLAX	0031	bu
Garlic	GARLC	0423	con
Ginseng, Root	GINR	0227	lbs
Gooseberries	GOOBR	0424	con
Grapefruit, Fresh	GFRFR	0205	con
Grapefruit, Juice	GFRJU	0204	con
Grapes	GRAPE	0053	ton
Grapes, Cabernet Franc	GRCBF	0646	ton
Grapes, Cabernet Sauvignon	GRCBS	0647	con
Grapes, Chardonnay	GRCHD	0648	con
Grapes, Chenin Blanc	GRCBL	0649	ton
Grapes, Gewurtztraminer	GRGWZ	0651	ton
Grapes, Grenache	GRGRN	0650	ton
Grapes, Merlot	GRMRT	0652	ton
Grapes, Muscadine	GRAMU	0285	ton
Grapes, Other Red Wine	GRORW	0654	ton
Grapes, Other White Wine	GROWW	0655	ton
Grapes, Processed	GRPPR	0680	ton
Grapes, Zinfandel	GRZFD	0653	ton
Guar	GUAR	0134	lbs
Guavas	GUAVA	0498	lbs
Guayule	GUAYU	0492	lbs
Hay, Alfalfa	HAYAL	0027	ton
Hay, Alfalfa - Brome Grass	HAABG	0681	ton
Hay, Alfalfa - Orchard Grass	HAAOG	0682	ton
Hay, Alfalfa - Timothy	HAATM	0683	ton
Hay, Bahalia Grass	HAYBG	0291	ton
Hay, Bermuda	HAYBU	0289	ton
Hay, Brome	HAYBR	0267	ton
Hay, Clover	HAYCL	0265	ton
Hay, Clover Silage	HAYCS	0415	ton
Hay, Coastal Bermuda	HAYBC	0394	ton
Hay, Colonial Bent Grass	HAYBT	0407	ton
Hay, Crabgrass	HACRA	0597	ton
Hay, Creeping Bent Grass	HAYBP	0408	ton
Hay, Fescue	HAYFC	0275	ton
Hay, Indigo	HAYIG	0440	ton
Hay, Lespedeza	HAYLS	0273	ton
Hay, Mixed	HAYMX	0296	ton
Hay, Native Grass	HAYNA	0379	ton

Hay, Oats and Peas	HAYOP	0588	ton
Hay, Oats and Vetch	HAYOF	0587	ton
Hay, Orchard Grass	HAYOG	0271	ton
Hay, Red Clover	HAYRC	0460	ton
Hay, Red Clover & Timothy	HAYCT	0684	ton
Hay, Ryegrass Annual	HAYRA	0430	ton
Hay, Ryegrass Perennial	HAYRP	0431	ton
Hay, Small Grain	HAYSG	0400	ton
Hay, Small Grain and Peas	HASGP	0598	ton
Hay, Soybean	HAYSB	0298	ton
Hay, Sudan Grass	SUDAN	0149	ton
Hay, Sudex	HAYSU	0269	ton
Hay, Sweet Clover	HAYSC	0461	ton
Hay, Tall Grass GT 25% Legume	HAYMO	0399	ton
Hay, Tall Grass LT 25% Legume	HAYTL	0398	ton
Hay, Timothy	HAYTM	0266	ton
Hay, Vetch	HAYVT	0434	ton
Haylage, Alfalfa	HAYAF	0614	ton
Hazel Nuts	HAZNT	0376	lbs
Hops	HOPS	0138	lbs
Horseradish	HORSE	0090	lbs
Jojoba	JOJOB	0490	lbs
Kale	KALE	0299	lbs
Kenaf	KENAF	0489	lbs
Kiwifruit	KIWIF	0463	lbs
Kohlrabi	KOLRA	0374	lbs
Kumquats	KUMQU	0473	lbs
Leeks	LEEKS	0377	lbs
Lemons, Fresh	LEMFR	0209	con
Lemons, Juice	LEMJU	0208	con
Lentils	LENTI	0401	lbs
Lettuce, Bibb	LETBB	0599	con
Lettuce, Head	LETUC	0140	lbs
Lettuce, Leaf	LETLF	0316	lbs
Lettuce, Romaine	LETRO	0331	lbs
Limequats	LIMEQ	0499	lbs
Limes, Fresh	LIMFR	0211	con
Limes, Juice	LIMJU	0210	con
Loganberries, Fruit	LOGBR	0481	lbs
Loquats	LOQUA	0500	lbs
Macadamias	MACAD	0469	lbs
Mandarins	MANDA	0474	con
Mangos	MANGO	0464	lbs
Marionberries	MARBR	0425	con
Marjoram	MARJO	0541	lbs
Melons, Canary	CAMEL	0483	lbs
Melons, Casaba	CSMEL	0484	lbs
Melons, Chinese Bitter	CBMEL	0512	lbs
Melons, Citron	CIMEL	0485	lbs
Melons, Crenshaw	CWMEL	0486	lbs
Melons, Honeydew	HONDW	0136	lbs
Melons, Persian	PEMEL	0487	lbs
Melons, Santa Claus	SCMEL	0488	lbs
Millet	MILET	0080	cwt

Mint	MINT	0402	lbs
Mullberries	MULBR	0370	con
Murcotts	MURCT	0055	con
Mushrooms	MUSHR	0403	lbs
Mustard	MUSTD	0130	lbs
Mustard Greens	MUSGR	0308	lbs
Nectarines, Fresh	NECFR	0251	ton
Nectarines, Juice	NECJU	0250	ton
Oats	OATS	0016	bu
Okra	OKRA	0286	lbs
Okra, Chinese	COKRA	0525	lbs
Olallieberries, Fruit	OLABR	0482	lbs
Olives	OLIVE	0501	con
Onion Sets	ONIST	0600	con
Onions	ONION	0142	cwt
Onions, Green	ONIGR	0319	lbs
Oranges, Blood & Toerh	ORABT	0477	con
Oranges, Fresh	ORAFR	0201	con
Oranges, Juice	ORAJU	0200	con
Oranges, Navel, Fresh	NAVFR	0215	con
Oranges, Navel, Juice	NAVJU	0214	con
Oranges, Temple, Fresh	TEMFR	0219	con
Oranges, Temple, Juice	TEMJU	0218	con
Oranges, Valencia	ORAVA	0476	con
Oregano	OREGA	0343	bun
Pak-Choi	PAKCH	0526	lbs
Paprika	PAPRI	0542	lbs
Parsley	PARSL	0320	lbs
Parsnip	PARSN	0338	lbs
Passion Fruits	PASFT	0502	lbs
Peaches, Fresh	PEAFR	0206	con
Peaches, Processed	PEAPR	0207	ton
Peanuts, Additional	PNTSA	0072	lbs
Peanuts, Green	PNTSG	0082	lbs
Peanuts, Quota	PNTSQ	0070	lbs
Pears, Fresh	PRSFR	0252	ton
Pears, Other Fresh	PEOFR	0656	ton
Pears, Other Processed	PEOPR	0657	ton
Pears, Processed	PRSPR	0253	ton
Peas, Austrian	AUPEA	0406	lbs
Peas, Bean	PEABN	0085	lbs
Peas, Black Eye	PEABE	0397	lbs
Peas, Butter	PEABU	0601	lbs
Peas, Dry	DPEAS	0067	lbs
Peas, Field	FLPEA	0288	lbs
Peas, Green	GPEAS	0064	lbs
Peas, Mini	PEMNI	0685	lbs
Peas, Purple Hull	PHPEA	0287	lbs
Peas, Snow	SNPEA	0321	lbs
Peas, Wrinkled Seed	WSPEA	0404	lbs
Pecans	PECAN	0146	lbs
Pecans, Improved	PEAIP	0624	lbs
Pecans, Native	PEANV	0625	lbs
Peppermint	PEPMT	0304	lbs

Peppers	PEPRS	0083	lbs
Peppers, Banana	PEPBA	0336	lbs
Peppers, Cherry	PEPCH	0337	lbs
Peppers, Hot (Jalapeno, etc.)	PEPHO	0221	lbs
Peppers, Pimento	PEPPI	0284	lbs
Peppers, Sweet (Bell, etc.)	PEPSW	0220	lbs
Peppers, Sweet, Fresh	PPSWF	0658	con
Peppers, Sweet, Processed	PPSWP	0659	con
Persimmons	PERSI	0465	lbs
Pistachios	PISTA	0470	lbs
Plumcots	PLUMC	0466	con
Plums, Fresh	PLUFR	0254	ton
Plums, Processed	PLUPR	0255	ton
Plums, Prunes	PRUNS	0147	ton
Pomegranates	POMEG	0467	lbs
Popcorn	POCRN	0043	lbs
Potatoes, Fresh	PATFR	0222	cwt
Potatoes, Processed	PATPR	0223	cwt
Potatoes, Sweet, Fresh	SWTFR	0260	cwt
Potatoes, Sweet, Processed	SWTPR	0261	cwt
Pumpkins, Fresh	PUMFR	0256	lbs
Pumpkins, Processed	PUMPR	0257	lbs
Quinces	QUINC	0468	lbs
Radicchio	RADIC	0530	lbs
Radishes	RADIS	0228	lbs
Rape Seed/Canola	RAPE	0129	lbs
Raspberries, Black, Fruit	RASBL	0301	con
Raspberries, Fall, Fruit	RASFL	0313	con
Raspberries, Red, Fruit	RASRD	0300	con
Raspberries, Red, Processed	RARPR	0310	lbs
Raspberries, Fall, Processed	RAFPR	0311	lbs
Rhubarb	RHUBR	0335	lbs
Rice	RICE	0018	lbs
Rice, Wild	RICEW	0641	lbs
Rutabaga	RUBAG	0339	lbs
Rye	RYE	0094	bu
Safflower	SFLWR	0079	lbs
Sage	SAGE	0344	bun
Salsify	SALSI	0532	lbs
Savory	SAVOR	0543	lbs
Seed, Alfalfa	SEEAL	0040	lbs
Seed, Alyce Clover	SEACL	0660	lbs
Seed, Anise	ANISE	0538	lbs
Seed, Asparagus	ASPFS	0545	lbs
Seed, Bahalia Grass	SEEBG	0292	lbs
Seed, Bahia - Argentine	SEBAR	0661	lbs
Seed, Basil	SEBSI	0686	lbs
Seed, Bean	SEBNS	0602	lbs
Seed, Bent Grass	SEBGS	0603	lbs
Seed, Bentgrass, Colonial	SEBTO	0687	lbs
Seed, Bentgrass, Creeping	SEBCR	0688	lbs
Seed, Bermuda Sprigs	SEEB	0293	lbs
Seed, Big Bluestem	SEEBB	0386	lbs
Seed, Birdsfoot	SEEBF	0356	lbs

Seed, Blue Grama	SEEBL	0445	lbs
Seed, Broccoli	BRCPS	0546	lbs
Seed, Brome	SEEBR	0268	lbs
Seed, Brown Top Millet	SEBTM	0662	lbs
Seed, Brussel Sprouts	BRUFS	0547	lbs
Seed, Buffalo Grass	SEEBU	0387	lbs
Seed, Cabbage	CABFS	0548	lbs
Seed, Canadian Wild Rye	SEEWR	0444	lbs
Seed, Collard	SECOL	0632	lbs
Seed, Canary	SEECY	0459	lbs
Seed, Cantaloupe	SECAN	0583	lbs
Seed, Carrot	CARSE	0452	lbs
Seed, Celery	CLERS	0549	lbs
Seed, Clover	SEECL	0264	lbs
Seed, Clover, Arrowhead	SEECA	0410	lbs
Seed, Clover, Crimson	SEECC	0411	lbs
Seed, Clover, Sub	SEECS	0413	lbs
Seed, Clover, White	SEECW	0414	lbs
Seed, Creeping Foxtail	SEEFX	0689	lbs
Seed, Crabgrass	SECRA	0604	lbs
Seed, Crown Veg	SEECV	0553	lbs
Seed, Cucumber	CUCFS	0550	lbs
Seed, Dill	SEDLL	0690	lbs
Seed, Dry Pea	SEDPA	0663	lbs
Seed, Egyptian Wheat	SEEEW	0591	lbs
Seed, Emerald Grass	SEMGR	0607	lbs
Seed, Fescue	SEEFS	0276	lbs
Seed, Fescue, Chewing	SEEFC	0419	lbs
Seed, Fescue, Red	SEEFR	0420	lbs
Seed, Fescue, Tall	SEETF	0384	lbs
Seed, Flat Pea	SEFPA	0605	lbs
Seed, Garrison Creeping Foxtail	SEEGF	0450	lbs
Seed, Ginseng	GINS	0089	lbs
Seed, Green Beans	SEGBS	0606	lbs
Seed, Green Needle Grass	SEEGN	0442	lbs
Seed, Hairy Grama	SEEHG	0390	lbs
Seed, Hybrid Cabbage	SEHCB	0575	lbs
Seed, Hybrid Sweet Corn	HSCRN	0062	con
Seed, Indian Grass	SEEIN	0388	lbs
Seed, Indigo	SEEIG	0441	lbs
Seed, Kale	SEKAL	0559	lbs
Seed, Kentucky Blue Grass	SEEKB	0262	lbs
Seed, Lespedeza	SEELS	0274	lbs
Seed, Lettuce	LETSE	0453	lbs
Seed, Little Bluestem	SEELB	0393	lbs
Seed, Lupin	SELUP	0608	lbs
Seed, Magnar Grass	SEMAG	0558	lbs
Seed, Mustard	SEMUS	0567	lbs
Seed, Native Grass	SEENG	0380	lbs
Seed, Old World Bluestem	SEEWB	0383	lbs
Seed, Onion	ONISE	0451	lbs
Seed, Orchard Grass	SEEOG	0272	lbs
Seed, Parsley	SEPAR	0568	lbs
Seed, Popcorn	SEPOP	0555	lbs

Seed, Pumpkin	SCPUM	0582	lbs
Seed, Radish	RADSD	0421	lbs
Seed, Red Clover	SEERC	0303	lbs
Seed, Redtop	SERDT	0691	lbs
Seed, Reed Canary Grass	SEERG	0449	lbs
Seed, Regar Brome	SERGB	0562	lbs
Seed, Rugby Bluegrass	SERBG	0669	lbs
Seed, Russian Wild Rye	SEERR	0447	lbs
Seed, Rutabaga	SERUT	0554	lbs
Seed, Ryegrass, Annual	SEARY	0665	lbs
Seed, Ryegrass, Perennial	SEPRG	0666	lbs
Seed, Safflower	SESAF	0585	lbs
Seed, Sainfoin	SESFN	0667	lbs
Seed, Sand Bluestem	SESBS	0692	lbs
Seed, Sand Lovegrass	SEESL	0389	lbs
Seed, Side Oats Grama	SEESO	0446	lbs
Seed, Slender Wheat Grass	SEESW	0443	lbs
Seed, Small Burnett Grass	SESBG	0557	lbs
Seed, Sugar Beet	SBESD	0432	lbs
Seed, Sweet Corn	SESWC	0560	lbs
Seed, Sweet Sorghum	SESSG	0609	lbs
Seed, Swisschard	SESWS	0610	lbs
Seed, Switchgrass	SEESG	0391	lbs
Seed, Tall Fescue	SEETF	0384	lbs
Seed, Tall Wheat	SEETW	0385	lbs
Seed, Timothy	SEETM	0263	lbs
Seed, Turnip	TRNSE	0455	lbs
Seed, Vetch, Common	SEEVC	0435	lbs
Seed, Vetch, Crown	SEEEV	0553	lbs
Seed, Vetch, Hairy	SEEVH	0436	lbs
Seed, Watermelon	SEWAT	0584	lbs
Seed, Weeping Lovegrass	SEELV	0382	lbs
Seed, Wheatgrass, Blue Bunch	SEBBW	0556	lbs
Seed, Wheatgrass, Crested	SEEWC	0412	lbs
Seed, Wheatgrass, Intermediate	SEEIW	0448	lbs
Seed, Wheatgrass, Pubescent	SEWPB	0664	lbs
Seed, Wheatgrass, Slender	SEESW	0443	lbs
Seed, Wheatgrass, Streambank	SEWSB	0668	lbs
Seed, Wheatgrass, Tall	SEETW	0385	lbs
Seed, Wheatgrass, Western	SEEWW	0392	lbs
Sesame	SESME	0396	lbs
Shallots	SHALL	0533	lbs
Shrubs, Ornamental	SHRUO	0328	ea
Silage, Popcorn	POPSL	0580	ton
Silage, Sorghum, Sweet	SISSW	0670	ton
Silage, Sudan Grass	SISGI	0671	ton
Silage, Sweet Corn	SWESL	0581	ton
Sorghum, Grain	SORGH	0051	bu
Sorghum, Sweet	SSORG	0050	bu
Soybeans	SOYBN	0081	bu
Soybeans, Lerado	SOYBL	0579	lbs
Spearmint	SPRMT	0305	lbs
Spearmint, Scotch	SPEAR	0672	lbs
Speltz	SPELZ	0131	lbs

Spinach, Fresh	SPIFR	0611	con
Spinach, Processed	SPIPR	0612	con
Squash	SQASH	0155	lbs
Squash, Gerber	SQGER	0578	ton
Squash, Summer	SQASU	0314	lbs
Squash, Winter	SQAWI	0315	lbs
Squash, Zucchini	SQAZU	0439	lbs
Strawberries	STWBR	0154	lbs
Sugar Beets	SBEET	0039	ton
Sugarcane	SCANE	0038	ton
Sunflower seed, non-oil	SUNFN	0151	lbs
Sunflower seed, oil	SUNFO	0153	lbs
Swisschard	SWCHR	0307	lbs
Tangelos, Fresh	TAGFR	0203	con
Tangelos, Juice	TAGJU	0202	con
Tangerines, Fresh	TANFR	0217	con
Tangerines, Juice	TANJU	0216	con
Tangors	TANGO	0478	con
Taro Root	TAROR	0535	lbs
Tarragon	TARRA	0544	lbs
Thyme	THYME	0345	bun
Tobacco, Burley	BURTB	0001	lbs
Tobacco, Cigar binder	CIBTB	0008	lbs
Tobacco, Cigar filler	CIFTB	0010	lbs
Tobacco, Cigar filler/binder	CFBTB	0007	lbs
Tobacco, Cigar wrapper	CIWTB	0012	lbs
Tobacco, Dark air-cured	DACTB	0005	lbs
Tobacco, Fire-cured	FICTB	0004	lbs
Tobacco, Flue-cured	FCTOB	0002	lbs
Tobacco, Maryland	MDTB	0009	lbs
Tobacco, Virginia fire-cured	VFCTB	0003	lbs
Tobacco, Virginia sun-cured	VSCTB	0006	lbs
Tomatoes, Cherry	TOMCH	0537	con
Tomatoes, Fresh	TMAFR	0224	cwt
Tomatoes, Processed	TMAPR	0225	cwt
Triticale	TRICL	0158	bu
Turnip Greens	TUPGR	0309	lbs
Turnips	TRNIP	0160	cwt
Walnuts	WLNUT	0029	con
Watercress	WACRE	0613	con
Watermelons	WATRM	0166	lbs
Wheat	WHEAT	0011	bu
White Sapote	WHSAP	0504	lbs
Yu Choy	YUCHO	0695	con

U.S. House of Representatives
Committee on Agriculture
Subcommittee on Wheat, Soybean and Feed Grain
Representative Dan Glickman, Chairman

Hearing on the Implementation of the 1988 Drought Legislation
March 23, 1988

Statement of
Texas Wheat Producer Association and Producer Board
Presented by
D.G. "Bill" Nelson, Executive Vice President

Mr. Chairman and members of the committee, my name is Bill Nelson. I am the Executive Vice President and Chief Administrative Officer of the Texas Wheat Producers Association -- the administrative and legislative liasion arm of organized wheat producers and of the Texas Wheat Producer Board -- the research, education and market development arm. There are 41,000 wheat producers in 220 of the 254 Texas counties.

Mr. Chairman, we commend this sub-committee, and the Congress for including "drought related" conditions as a part of the 1988 Drought Legislation. This was important to many Texas producers. At harvest time many had in excess of 100% of their normal rainfall, yet had severe losses due to earlier dry conditions in January and February. This produced weakened plants that could not resist disease, insect and other maladies.

My purpose here today is to report that similar drought-related damage as well as pure drought damages is worse now than at this time a year ago. The Agricultural Statistics Service reported on March 19th, that the Texas wheat crop was 46% of normal as compared to 65% of normal this date in 1988. The crop is reported to be 1% excellent, 8% good, 50% fair, 38% poor and 3% very poor. Statements are attached which have been obtained from Texas Extension Agronomists and Entomologists that indicate that disease, insects and freeze all were enhanced in their damage by drought conditions. In fact, the rain fall in the Texas Panhandle fifty year average is nearly four inches during the wheat growing period from October through February. This year it is only slightly over one inch. All this is to say that many individual wheat producers are in worse shape this year than last due to drought and drought-related conditions. This is to request that this sub-committee consider extending provisions of the 1988 Drought Legislation into 1989.

While pleading the case of the individual producer in Texas and other areas of the Southwest, we want to stress the fact that our domestic or international consumer should not be concerned. The U.S. will not have a wheat crop production report until May, but the International Wheat Council is projecting the 1989 wheat crop at over 2 billion bushels. This level along with the projected June 1 carry-in stocks of 534 million bushels will assure an adequate supply to meet our domestic and export needs and add almost a 100 million bushels to the June 1990 carry-over supply.

Thank you for the opportunity to bring these facts before the committee.

(Attachments follow:)

Texas Agricultural Extension Service

The Texas A&M University System
350 Soil and Crop Sciences
College Station, TX 77843-2474

March 15, 1989

Mr. Bill Nelson
Executive Vice President
Texas Wheat Producers Association
625 Texas Commerce Bank
Amarillo, TX 79109

Dear Bill:

Enclosed is a synopsis of the Texas wheat crop condition as I am informed on this date. The crop as a whole, particularly the crop west of a line from Victoria to Denton has been damaged by varying degrees of drought. The drought, coupled with unusually warm weather through January has been subjected to unusually high pressures from greenbugs. The combination of drought aphid damage and advanced maturity due to warm winter weather set us up for unusually high losses from winter kill from the two periods of record cold in February and March. Barring extremely favorable weather conditions during the remainder of the crop production season, I look for another harvest under 90 million bushels, despite the 0.5 million acre increase in planting this year.

Bill, these are just a few comments and generalizations I have made in the short time allotted. If I can be of further service, please don't hesitate to call me.

Sincerely yours,

Travis D. Miller

Travis D. Miller
Extension Agronomist
-- Small Grains and Soybeans

TDM:dga

Texas Wheat Crop Situation
March 15, 1989

Dr. Travis D. Miller
Extension Agronomist -- Small Grains & Soybeans

South central and southwest (Districts 10 & 13)

Moisture was very limited at planting time. Many producers in this region had to replant more than once, as early moisture was inadequate to get a uniform stand. Rainfall in late December and early January improved the crop condition somewhat. Subsurface moisture remains critically short. Two extremely cold weather patterns in early February and early March killed 10 to 50% of the wheat and over half of the oats in these counties. Freeze losses from the February freeze were much more severe in the drier areas . Northern areas of District 10 are in much better shape for moisture than the remainder of this region.

Central and north central (Districts 4 & 8)

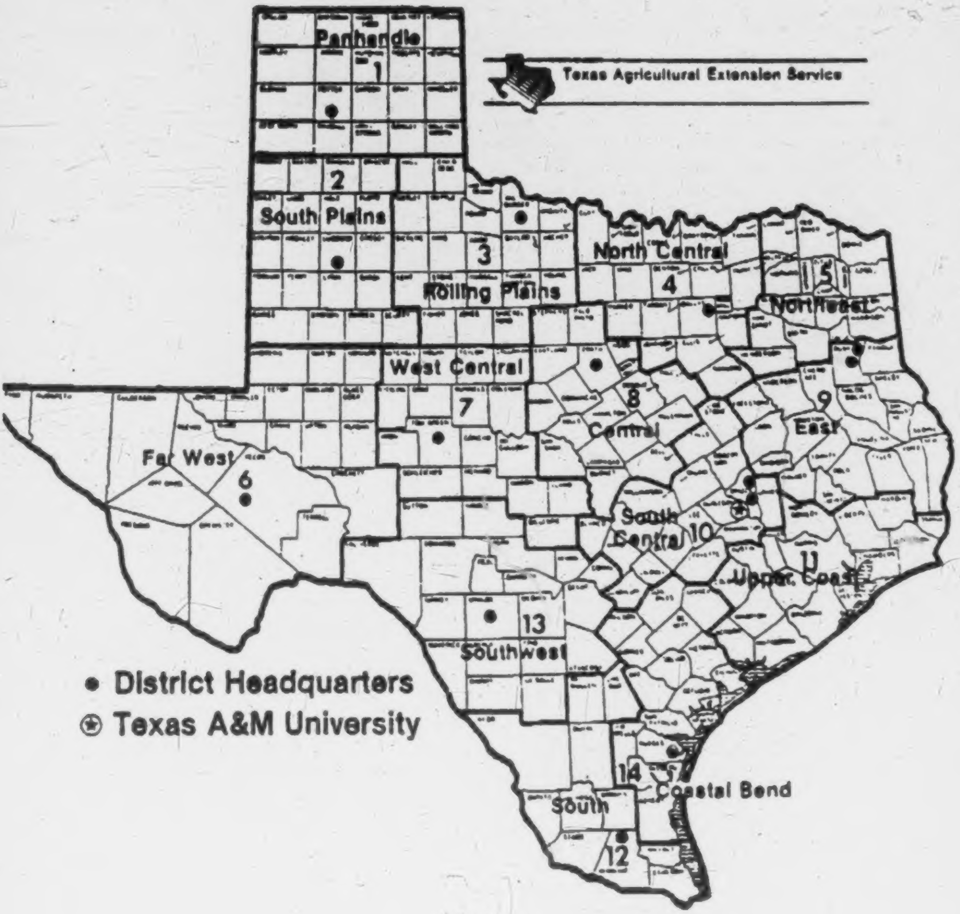
Moisture has been very limited in the western reaches of these districts. Moisture was short at planting time in the eastern areas, but adequate rains in November through January have alleviated most of the droughty conditions in this region. Stands were poor in the west and suffered until good February rains brought relief to much of this region. Stocker operators in the west have had very little grazing due to very short moisture during the fall. Crop conditions improved somewhat with the February rain, but subsurface moisture is still quite short over much of the region. The wheat crop from Waco north has looked above average over much of the growing season due to mild weather and adequate moisture. Hard freezes in February and in March killed early wheat varieties resulting is a loss of 10 to 20% in many areas. Snow cover in the March freeze reduced losses of jointed wheat.

West central and rolling plains (Districts 3 & 6)

Much of this region received 3 to 5 inch rains from Hurricane Gilbert in September. Early planted wheat got off to a good start, but warmer weather and the total lack of rainfall over the next 5 months severely reduced wheat yield potential. Most cattle were removed from wheat pastures at least 2 months ahead of normal due to dry conditions and the lack of forage. Some of the region received good rains in February, but rainfall amounts were inadequate to replenish subsurface moisture. Wheat stands are poor and freeze injury in early maturing wheat varieties is widespread. Foot rot, which was aggravated by warm, dry weather early, followed by extreme cold weather in February and March, is the worst that has been observed in years. Greenbug pressure has been abnormally severe due to dry, warm winter weather. Freeze injury is much greater in fields affected by the combination of drought and greenbug pressure.

South Plains and Panhandle (Districts 1 & 2)

Many of the same conditions that exist in the rolling plains are prevalent in Districts 1 and 2. Adequate surface moisture was available at planting. Prolonged warm weather through January promoted greater than normal vegetative growth during the fall and early winter so that available moisture was rapidly exhausted. Moisture has been so short here that cattle had to be removed from most dryland wheat by early January when the normal livestock removal date is March 1. Fall and winter greenbug and mite pressure have been very high due to warm weather and droughty conditions. The exact amount of winter-kill of wheat has not yet been determined, as green-up has been slow due to abnormally cold February weather. Winter-kill is much greater in dryland wheat, particularly that which had heavy, uncontrolled greenbug population. The extremely dry conditions coupled with freeze and insect activity has substantially reduced yield potential of Panhandle wheat.


Texas Agricultural Extension Service
Panhandle
1
2
South Plains
3
Rolling Plains
North Central
4
5
Northeast
West Central
7
8
Central
9
East
Far West
6
South Central
10
11
Upper Coast
13
Southwest
14
Coastal Bend
South
12
● District Headquarters
⊛ Texas A&M University

Texas
Agricultural
Extension
Service

The Texas A&M University System

March 17, 1989
6500 Amarillo Blvd. West
Amarillo, Texas 79106

Mr. Bill Nelson
Executive Vice President
Texas Wheat Producers Board
803 Texas Commerce Bank
2201 Civic Circle
Amarillo, Texas 79109

Bill:

In early October economically damaging greenbug infestations were present in many wheat fields of the north central Texas Panhandle. By early November, with continued mild fall weather conditions, the greenbug problem had spread throughout the Texas Panhandle.

Weather cold enough to halt or slow greenbug development failed to arrive by late November or early December. The greenbug infestation continued to increase to record proportions. Wheat producers applied insecticides to control the greenbugs until cold weather arrived. Those conditions did not come until early February.

Drought conditions that have existed since October stressed the wheat and exacerbated the damage brought by greenbug. The effect of drought and greenbugs have combined to have a devastating impact on area wheat production.

Sincerely,

Carl D. Patrick

Dr. Carl Patrick
Extension Entomologist

CDP:lf

Texas Agricultural Extension Service
The Texas A&M University System

March 16, 1989
6500 Amarillo Blvd. West
Amarillo, Texas 79106

Mr. Bill Nelson
Executive Vice President
Texas Wheat Producers Board
803 Texas Commerce Bank
2201 Civic Circle
Amarillo, TX 79109

TOPIC: TEXAS PANHANDLE WHEAT UPDATE

Bill:

Most of the wheat throughout the area remains in poor condition. The primary reason for our wheat being in its present condition can be related to the lack of precipitation received over the last five to six months. (See Table). Since October 1st, we have received only about a third of our normal precipitation.

Lack of moisture, especially during October and November, led to poorly developed root systems. Because the wheat was not well rooted, cattle placed on the wheat for grazing were able to pull a lot of wheat up.

Further stress was placed on the wheat during the fall months by unusually high populations of greenbugs. Because of exceptionally mild temperatures during November and December the greenbugs were able to survive and feed on the wheat throughout most of the fall and early winter months.

January and February also contributed to the poor condition of area wheat. High temperatures caused wheat to begin growing, breaking its winter dormancy. The high temperatures were then followed by two hard freezes, two weeks apart, with warm temperatures in between. The warm temperatures caused the wheat to be more susceptible to freeze injury. In some cases, the cold temperatures were the final blow to the crop resulting in death of the wheat.

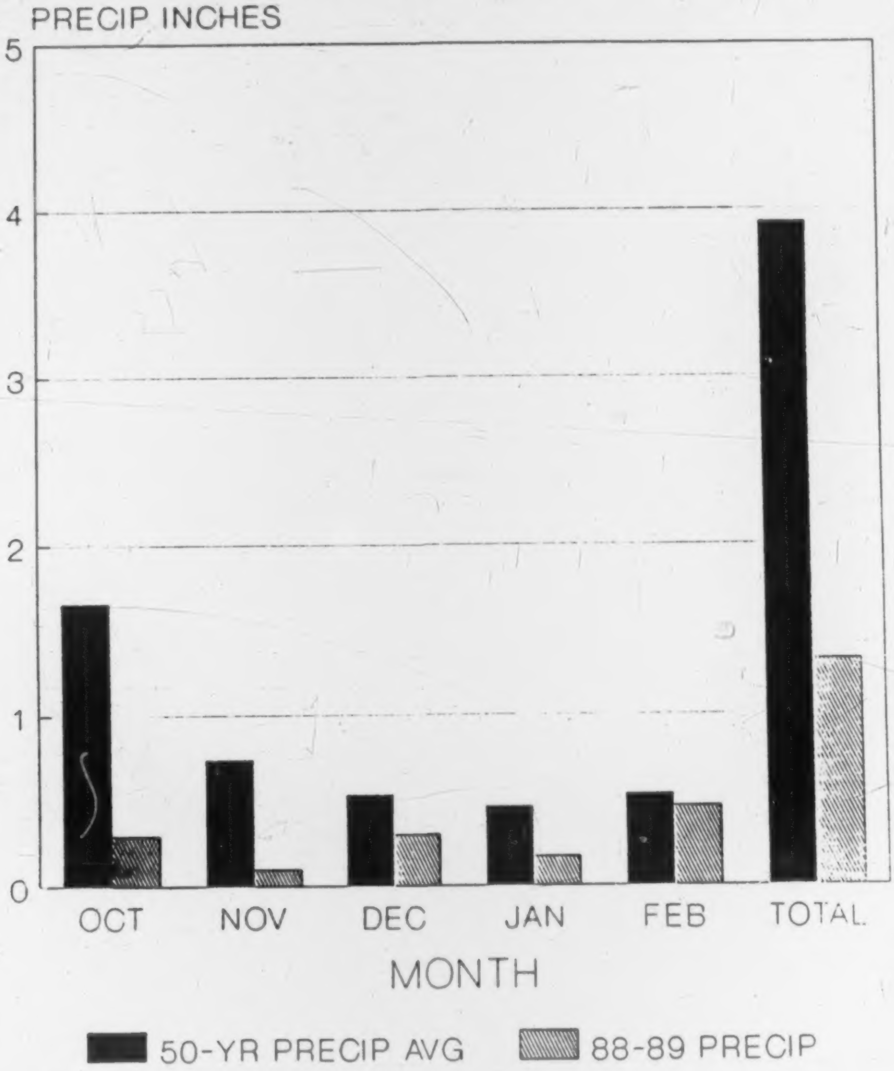
Stressed wheat is also more susceptible to insect and diseases. Under the present conditions we can expect further damage to the wheat crop to occur as spring weather encourages the development disease infection and insect infestations in our area wheat.

Sincerely,

Dr. Brent Bean
Extension Agronomist

BB:lf

PRECIPITATION FOR 88-89 WHEAT CROP



NCA

NATIONAL
CATTLEMEN'S
ASSOCIATION

1301 Pennsylvania Avenue, N.W.
Suite 300
Washington, D.C. 20004
(202) 347-0228

TESTIMONY

on behalf of

NATIONAL CATTLEMEN'S ASSOCIATION

before the

U.S. House of Representatives
Agriculture Committee
Wheat, Soybean and Feed Grains Subcommittee

March 23, 1989

on

Implementation of 1988 Drought Relief Legislation

by

G. Chandler Keys, III
Director, Congressional Relations

The National Cattlemen's Association is the national spokesman for all segments of the beef cattle industry--including cattle breeders, producers and feeders. The NCA represents approximately 230,000 cattlemen. Membership includes individual members as well as 49 affiliated state cattle associations and 23 national breed associations.

Mr. Chairman, thank you for allowing the National Cattlemen's Association to participate in this hearing. My name is Chandler Keys and I am NCA's Director of Congressional Relations.

A short time ago, this Committee room was full of Congressmen, USDA officials, Congressional staff, farm and commodity associations, reporters, and ranchers and farmers all engaged in a grand effort to produce legislation. The legislation, as we all know, became the Drought Assistance Act of 1988. No one was expecting the drought, but reaction time was swift and the government responded expeditiously.

Livestock, especially grazing livestock, are the first to feel the effects of drought. Pastures and watering holes dry up and farmers and ranchers are forced to provide expensive feed at a time of year when they least expect it.

NCA believes the USDA did an admirable job early on in instituting programs and projects to alleviate the burden of the drought on the livestock industry. By allowing haying and grazing on set-aside acres, haying the CRP, implementing the existing emergency feed programs, purchasing red meat to ease the market pressure from added cow slaughter, the USDA helped ease fears of wholesale livestock slaughter. Excessive slaughter would have been a disaster especially since the U.S. now has the smallest cow herd in almost 40 years.

The Drought Assistance Act of 1988 was developed to give USDA added statutory authority to further help American farmers and ranchers. The Act basically covered two categories of assistance, one for crops, the other for livestock. NCA helped formulate the livestock feed provisions and was pleased with the final product. Livestock producers throughout the drought stricken areas are benefitting from the Act and are grateful. Congress deserves the credit.

No major catastrophes have occurred and this is probably directly attributable to county ASCS officials going that extra mile to make the program work. I would, however, be remiss if I did not elaborate USDA's problems, misunderstandings, foul ups and general disregard for the intent of Congress, while propagating regulations for the emergency livestock feeding programs.

First, it took USDA nearly two months from enactment date, August 26, 1988, to issue interim regulations for the emergency feed programs. (The crop disaster program regulations took less then a month). Local ASCS offices were acting in the dark and mass confusion ensued. NCA along with the National Pork Producers, American Feed Industry Association, the American Farm Bureau, National Milk Producers, the Grange, Turkey Federation and the United Egg Producers urged Secretary Lyng to publish the interim regulations in a letter, the regulations were finally published October 14th.

Listed below are a few of NCA's grievances with the livestock feeding programs implemented by USDA.

I. Reimbursement of cost incurred for installing emergency livestock water projects.

NCA strongly believed this discretionary program needed to be implemented because the current water program, the Emergency Conservation Program, had limited funding and time constraints. It is well known that the ECP is continually under-funded and those funds are almost always spent immediately on a first-come-first serve basis. Another hindering factor of the ECP is that water projects must be approved before construction can take place. Usually, the livestock producer is unaware of the ECP until after his water project is completed, at which time the producer is ineligible for reimbursement. NCA recommended that the USDA implement the new water project program so livestock producers could be reimbursed for their emergency livestock water projects. It was clearly the intent of Congress to help all livestock producers recoup some of their cost for emergency water projects, not just those who were informed about the ECP. Obviously, this is a fairness issue.

II. Livestock Transportation Assistance

Congress developed the Livestock Transportation Assistance Provision in the legislation to address reimbursement to livestock producers who, because of the lack of pasture, hay or feed, were forced to move their cow herds to distant forage sources. This unprecedented movement of cow herds took place during the height of the drought. Cattlemen transported their "core" cow herds out of the Dakota's and Eastern Montana to greener pastures in Nebraska and Kansas. Cattlemen resorted to abnormal management patterns in order to preserve their cow herds.

To help these cattlemen meet expenses, NCA asked USDA to implement the Livestock Transportation Assistance Provision. The number of cattle moved as a result of the drought may not be enormous, but the cost to the individual was prohibitive. Share assistance of at least 50/50 cost, for one leg of transportation by the USDA, would have helped these industrious cattlemen overcome the burdensome trucking cost. The USDA declined to implement the program.

III. Income Restrictions

In reference to the gross revenue limitation, we have two observations. We should premise our comments on this area by stating we did not oppose a gross income threshold and recognize the political force which created the limitation.

First, we feel the cost of purchased livestock should be subtracted from the gross income before applying the $2.5 million test. A farmer feeder who buys 600 to 700 pound steers and sells them at 1,000 to 1,100 pounds should not be forced to apply all gross proceeds from the steer for purposes of the $2.5 million test. Without the cost of purchased livestock subtracted, many family farmers will be unintentionally prohibited from receiving assistance.

Second, many farmer feeders and cattlemen made sound business and management decisions during the early summer of 1988, by enrolling in the existing feed assistance programs. At that time the law did not provide for the $2.5 million gross income cap. Congress recognized this problem and included legislative language, section 604 (d), which stated eligibility established before the enactment of the Act will be grandfathered. We asked the USDA that this language be judiciously implemented. They declined to state that while these producers were certainly eligible, they no longer qualified.

IV. Animal Unit

The unwillingness of USDA to address the question of the formula used to compensate 1.00 animal unit is frustrating. The 1.00 animal unit of 10 pounds of feed a day was formulated in the 1940's when the average beef cow weighed less than 900 pounds. Today's beef cow often weighs over 1,100 pounds therefore calling for more upkeep in the form of feed. USDA has acknowledged the growth of dairy cows by increasing their dairy unit by 0.5 over the past year. NCA requested a review of the information used to compute the "animal unit." NCA strongly feels the USDA must justify their current animal unit formula or adjust the unit to better reflect today's beef cow.

V. CRP Acres

NCA formally petitioned the USDA to open CRP acres for grazing in drought areas. They declined sighting major opposition from environmental groups. Environmentalists feared over-grazing and wildlife destruction even though haying of these acres had been approved months earlier.

It bewilders NCA how a cow can be perceived as more destructive to a field of grass than an indiscriminate hay mower. We doubt many farmers can sight an incident of a cow stepping on a pheasant but we are sure many can attest to a hay machine cutting through a nest of bird eggs.

We hope USDA will not discriminate against grazing in the future based on such frivolous arguments.

VI. Other Problems

A. Crop insurance counted against your application for emergency feed. It is not for crop disaster payments.

B. Some county ASCS offices were requesting to keep a permanent file of applicants financial holdings.

C. Limited knowledge in county, state and Washington D.C. ASCS offices of how the cattle industry functions. Misunderstanding financing, classes of cattle, and general animal care are some of the problem areas.

D. A NCA member denied eligibility in Illinois because the cut-off date for requesting pasture loss was November, 1988, but, he could not apply until his on-hand feed supply ran out in January, 1989.

NCA believes the Drought Assistance Act of 1988 was a good effort by Congress to help alleviate some of the financial hard times facing farmers and ranchers during this past year. For the most part USDA, especially early on, used their resources efficiently.

However, we know a much better job could have been done in implementing the livestock assistance programs. Some of the blame must be laid at the feet of OMB but, the USDA did not fight hard enough for the people they serve. ASCS must deter from the mind set that every farmer/rancher is a crook or a cheat, this only breeds resentment and lack of faith between Washington and the country.

For all the good intentions in the drought bill, it may be for naught with many livestock producers because of the lack of good follow through and good faith on the part of the USDA.

STATEMENT OF THE

AMERICAN FEED INDUSTRY ASSOCIATION

before the

SUBCOMMITTEE ON WHEAT, SOYBEANS & FEED GRAINS

HOUSE AGRICULTURE COMMITTEE

on

MATTERS CONCERNING THE 1988 DROUGHT &

THE DISASTER ASSISTANCE ACT OF 1988

Steve Kopperud
Vice President-Legislation

March 23, 1989

Chairman Glickman and members of the committee, I am Steve Kopperud, vice president-legislation for the American Feed Industry Association (AFIA). AFIA thanks you for the opportunity to comment on matters related to the Disaster Assistance Act of 1988.

It was this legislation which, for the first time in more than a decade, made substantial, necessary changes to permanent law authorizing emergency feed assistance programs to livestock producers. Within the parameters of that discussion, AFIA would like to specifically address the issue of emergency livestock feed assistance.

AFIA is a national trade association representing the manufacturers of more than 70% of the primary formula poultry and livestock feeds sold annually in the U.S. The domestic feed industry also purchases $12-15 billion worth of feed ingredients a year, mostly grain and grain byproducts, making it the nation's single largest user of domestically produced grains. Our membership also includes those companies supplying animal drugs, ingredients, equipment and services to feed manufacturers.

AFIA commends this subcommittee, the full committee and the Congress for its timely action to provide emergency feed assistance to affected producers following the devastating drought of 1988. We further commend Chairman Glickman and the subcommittee for this very timely review of these programs to insure they continue to meet the needs of the American farmer. AFIA would also like to recognize the efforts of the U.S. Department of Agriculture in responding to the needs of drought-stricken areas.

AFIA's involvement in emergency feed assistance programs dates back to Sec. 407 of the Agriculture Act of 1949, which authorizes the Secretary of Agriculture to permit feed dealers and manufacturers to forward discounted feed from their inventories in return for title to emergency assistance grain from eligible farmers. Our involvement in subsequent emergency actions, both on Capitol Hill and through USDA has continued through the last four decades.

AFIA's contributions to the Disaster Assistance Act of 1988 actually began prior to last summer's drought. In the spring of 1988, several California members contacted our offices to explain that there appeared to be an oversight in the limited regional emergency feed program operating in California due to the previous season's drought. State ASCS officials were allowing cost-sharing only on liquid feeds and supplements and not on dry supplements, creating a dramatic market imbalance and penalizing producers who used dry supplemental feeds. AFIA met with ASCS in Washington, and the agency administratively moved quickly to include all eligible products for cost-sharing assistance in that regional program.

As congressional efforts began on crafting a legislative relief package for drought-affected farmers, AFIA brought its experience on such legislation to the table in the early stages of bill drafting. AFIA's requests were as follows:

--First, AFIA supported inclusion in the bill of the feed dealer/manufacturer option, which allows the federal government to use the private feed distribution infrastructure already in place in rural America to forward commercial feeds almost immediately to eligible farmers.

--Second, AFIA suggested that--as in past administrative relief programs--farmers should be allowed to use Payment-in-kind (PIK) certificates as currency in dealing with feed companies, local elevators, and other suppliers.

--Finally, AFIA suggested the definition of "eligible feed" under the 50/50 cost-sharing program be expanded to include premixes, dry supplemental feed and oilseed meals. Expanding the definition of "eligible feed," and hence eligibility for feed assistance, to the full range of modern commercial feed products allows farmers to receive cost-share without interfering with traditional feeding practices. In the past, when cost-share was limited, market balance in the feed industry was disrupted as farmers were arbitrarily switched from traditional feeding practices to those products which were cost-shared.

With strong livestock producer group support for these recommendations, AFIA supplied suggested legislative and report language to both House and Senate Agriculture Committee members and worked with staff to refine this language.

Due in large part to unified livestock producer support, AFIA's recommendations were included in the final draft bill, the legislation approved by the House, and ultimately the compromise bill approved by the full Congress.

AFIA remained active with emergency feed assistance issues while USDA prepared regulations to implement the programs. AFIA filed official comment on the Oct. 14, 1988, interim rule, and continued to provide USDA with information and support.

We were dismayed at the length of time it took USDA to publish its interim rule. The legislative and report language were both explicit and the changes being made to existing programs were not necessarily that extreme.

The frustration among livestock producers groups, AFIA and others over how these new programs would be implemented culminated in a joint letter to Sec. Richard Lyng, dated Oct. 4, 1988, and signed by the American Feed Industry Assn., the American Farm Bureau Federation, the National Cattlemen's Assn., the National Grange, the National Milk Producers Federation, the National Pork Producers Council, the National Turkey Federation, and the United Egg Producers.

The delay in publishing the Oct. 14 interim rule caused general confusion in the field over program implementation. At one point, a midwest ASCS official reportedly told producers that as much information as he had on the new program provisions was a customer bulletin from a major feed company.

While, as we've said, the law was explicit as to producer and product eligibility, many state and local ASCS offices did not--for whatever reason--begin implementing any of the new provisions, despite the Aug. 26 effective date, until the rules were published. This was the beginning of major confusion in the country.

Despite the highly professional work of national ASCS officials, AFIA member companies and many producers ran into major problems with implementation of the drought program in the field. While ASCS communications to state and county ASCS offices appeared clear and concise, local ASCS officials seemed confused, hesitant or unwilling to implement the expanded programs.

Of particular problem seems to be the definition of the term "eligible feed," especially when it came to dealing with premixes.

AFIA found this curious, since in the House-passed version the report was fairly straight-forward:

"Premix-type feed, generally defined as a formulation of ingredients, such as vitamins or minerals, designed to be mixed (on or off-farm) with grain or protein ingredients to create a balanced ration." (Report 100-800, Part I, July 27, 1988, page 73)

(It is understood that the compromise legislation's report did not include a specific premix definition; however, the House report on H.R. 5015 as part of the legislative history on the program changes should have been the agency's guide.)

On Nov. 3, 1988, AFIA contacted Emergency Operations & Livestock Programs at USDA/ASCS about the confusion. At that time AFIA member companies were reporting county ASCS officials were telling livestock owners that:

1) ASCS only cost-shares on complete feeds,

2) As producers they would receive greater assistance by shifting from on-farm mixing of feeds to the purchase of complete feeds.

Such counseling by local ASCS officials caused exactly the kind of market disruption and producer confusion the Congress attempted to avoid. AFIA requested that ASCS provide state ASCS officials with clarification of the agency's explanation of the cost-share on premix products.

ASCS responded quickly with Notice DF-177, dated Nov. 9, 1989. The notice attempted to clarify the confusion surrounding the definition of premix. However, problems in the field continued. In addition, the definition of premix given in DF-177 still left some questions unanswered.

ASCS acted again in Dec. 6, 1988, issuing Notice DF-179, which clarified the definition of premix further. AFIA representatives met with ASCS officials on Dec. 13 to discuss DF-179, and problems that still remained. At that time, AFIA was asked for additional comment on the entire premix definition issue, as well as related information on the total dietary nutritive value of certain forages and roughages. This was provided in a letter dated Dec. 23.

As we continue to wait for the final rule--a draft of which is apparently under review by the USDA Office of General Counsel--problems in the field continue to occur. Recently, a state official in Wisconsin told AFIA member-companies that they would no longer cost-share on premixes that include yeast.

And just yesterday, a Virginia farmer contacted AFIA's Washington office wanting to know why, if his neighbors in

West Virginia and North Carolina were receiving cost-share on premixes, his local ASCS board was denying him the same assistance.

AFIA recognizes that many of the instances we have heard may be due to producer misunderstanding of who and what is eligible, and possibly to an even larger degree, what is not eligible for assistance. However, this speaks to the inadequate communication between the federal government and those most directly affected by these programs.

We are totally supportive of the ASCS emergency livestock program staff; their doors were always open, and they were always willing to discuss these matters with us.

However, we continue to have some kind of communications gap between ASCS-Washington and some of the state ASCS offices and apparently most of the county ASCS offices.

Despite ASCS communications to the country, we have noted that in many cases, some state and local committees show little interest in learning the details of the program changes. Speculating on the reasons--from departure from traditional programs to the minor increase in calculations and paperwork to figure premix and supplement product cost-sharing--is futile. Whatever the reason, despite the efforts of Congress and USDA officials in Washington, DC, emergency feed assistance programs are not being implemented correctly in many counties and states across the nation. The ultimate loser is the producer trying to get back on his feet after last summer's devastating drought.

AFIA has provided copies of the various ASCS directives and our communications with ASCS in an attempt to rectify this confusion.

Again, AFIA thanks the committee for their attention to emergency feed assistance programs, problems, and concerns. We appreciate the opportunity to comment. We stand ready to assist the committee in any way we can to address the feed needs of livestock and poultry owners in drought-stricken areas.

(The prepared statement of the American Feed Association before the Senate Committee on Agriculture, July 12, 1988, is held in the committee files.)

NATIONAL PORK
Producers Council®

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Statement of the

NATIONAL PORK PRODUCERS COUNCIL

Before the

Subcommittee on Wheat, Soybeans & Feed Grains

Committee on Agriculture

U. S. House of Representatives

on

Implementation of the Disaster Assistance Act of 1988

March 23, 1989

Presented by: Don Gingerich, President
National Pork Producers Council
Parnell, Iowa

Mr. Chairman and Members of the Committee:

I am pleased to have this opportunity to testify before you today on the Disaster Assistance Act of 1988. As President of the National Pork Producers Council (NPPC), I want to personally thank you for your support of the pork industry in the past. The members of the committee and staff were particularly helpful in developing drought legislation last year, and we cannot say enough good things about your efforts to assist pork producers.

I will be testifying on behalf of NPPC which represents 100,000 pork producers and their families in 45 member states that are affiliated with the national organization. NPPC is the largest commodity dues-paying organization in the United States and accounts for more than 90 percent of the nation's commercial pork production.

Although we believe that the future of our industry is in our own hands, pork producers are convinced that we will need the cooperation of the federal government in certain situations, such as last year's devastating drought.

We are not here today to belabor any issues that are now behind us concerning how the disaster assistance program has been administered. But, we do believe the Committee needs to know how effective the drought relief legislation was in helping our producers in an extremely serious time of need. Simply stated, the relief provided through the U.S. Department of Agriculture has been less than acceptable to pork producers. Most producers either were deemed to be ineligible for the feed assistance programs or, if they were eligible, the level of assistance provided was usually negligible.

As of February 28, 1989, only $243 million in Emergency Feed Program benefits had been distributed to all livestock producers including beef, dairy, lamb, and pork producers. In addition, only 514 million pounds of feed (which translates roughly to $25-$30 million in feed assistance) were distributed under the Emergency Feed Assistance Program. These actual outlays to livestock producers are far short of the original estimates presented to Congress. During the debate on the Disaster Assistance Act, it was estimated that approximately $800 million would be distributed annually to livestock producers in 1988 and 1989.

It is obvious that the emergency feed programs are not designed to reimburse livestock producers for their actual losses. Crop assistance payments, in contrast, are designed to reimburse crop producers for financial loss where possible. Livestock producers only receive feed assistance to provide a survival ration of feed to keep their animals alive.

Under the crop disaster assistance program, crop producers have received $2.47 billion (as of February 28, 1989). The discrepancy in treatment relegates livestock producers to the status of second class citizens.

Part of the problem with the emergency feed programs is that the livestock rations reflect conditions in agriculture some 40 years ago. These rations are no more suitable today than a two-row corn planter is for a farmer with a 2,000-acre farm.

For a full grown sow, pork producers are allocated a survival or sustenance ration of 3.3 pounds of feed per day. For swine less than 6 months old, the eligible pork producer looks forward to a ration of 2 pounds of feed per day. Feed rations for other livestock species are also outdated. Producers were only eligible for 20 pounds of feed per day for each dairy cow, 10 pounds per day for other cattle more than a year old and 5 pounds per day for cattle 6 months to one year old.

I urge this Committee to challenge the Department of Agriculture to find one pork producer anywhere that will say that 3.3 pounds of feed per day is sufficient or even humane when that 500-pound animal is suffering from 95-degree heat and no water. Clearly, we as pork producers believe that the feed ration is extremely low and in some cases possibly inhumane for animals. We ask that this Committee work to ensure that livestock producers obtain a fair ration of feed.

Unlike cattle or sheep, hogs are not forage animals that allow pork producers to use a haying or grazing option. Other than the emergency feed programs, our only available alternative during last year's drought was to harvest set-aside acres. Given the severity of the drought, we asked the Secretary of Agriculture on June 22, 1988 to allow our producers the opportunity to harvest oats on set-aside acres. Although this request was denied, cattlemen were granted the opportunity to hay and graze set-aside acres and harvest Conservation Reserve Program acres.

Last summer, the Secretary of Agriculture announced the availability of the Emergency Feed Assistance Program based on authority provided in 1949 legislation (7 U.S.C. 1427). This authority, however, only provided assistance for cattle (including dairy cattle) sheep, and goats. It did not make provision for pork producers to be eligible for assistance for their swine. In other words, prior to last year's drought relief legislation, pork producers were not eligible for the Emergency Feed Assistance Program that allowed livestock producers to receive grain at 75 percent of the county loan rate. It appears that the Secretary of Agriculture had the authority under Pub.L. 86-299, Sept. 21, 1959, 73 Stat. 574, amended Pub.L. 88-585, Section 3, Sept. 11, 1964, 78 Stat. 927 "to sell, at not less than the current basic county support rate...any wheat, corn, oats, barley, rye, or grain sorghums...owned by the Commodity Credit Corporation...to provide feed for livestock" in an emergency area. Therefore, it allowed all livestock producers, including pork producers, to be eligible for assistance at a level of 100 percent of the county loan rate.

Because approximately 20-to-25 percent of our producer members do not grow their own feed, we requested that they also be eligible for feed assistance under the new drought legislation. Many of these producers (that do not raise their own feed) are being penalized for making the best use of their resources. We have members with limited opportunities to grow their own grain because they farm hilly land. Others are struggling to make a start and don't own large acreages of cropland. It is hard to comprehend how providing assistance to these producers could cost $2 billion as estimated by the Office of Management and Budget.

The whole program for all other livestock producers amounted to an outlay of less than $300 million.

It appears that ASCS has interpreted the emergency feed programs so narrowly, that only a few pork producers are eligible. Although Section 1763(a) of the 1985 Farm Bill, and report language included in the Disaster Act of 1988, specifically state that feed must be suitable for the particular animal, ASCS continues to interpret the law in such a fashion to use surplus hay or pasture as their reason to deny pork producers access to benefits they deserve. For example, a pork producer with excess pasture and/or hay with 3,000 pigs and two 4-H cows is denied eligibility for the emergency feed programs. Either his few cows are to make use of all the surplus pasture or hay, or the livestock producer is required to rent the pasture or sell the hay. Surely, ASCS would be able to calculate how much pasture or hay could be used by the two cows in this example.

We are also concerned that federal crop insurance indemnity payments will be treated as feed on hand. To convert the value of crop insurance payments to a grain equivalent only works to minimize a livestock producer's eligibility for feed assistance. Livestock producers who had the foresight to purchase federal crop insurance to help minimize the adverse affects of crop failure should not be penalized when it comes to eligibility for the emergency feed programs. It is unfair to translate federal crop insurance payments for livestock producers to feed on hand, while producers that purchased private crop insurance are not denied drought relief benefits if they had purchased crop insurance.

There is also an anomaly in regards to cost-share assistance on transportation of feed. It does not make sense to penalize the producers who have attempted to reduce costs by taking possession of the feed at the seller's location and transporting it themselves. The program has discouraged private initiative and not allowed cost-sharing reimbursements for this effort. Clearly, it is inequitable to limit Emergency Feed Program assistance to the purchase price paid by the producer at the point of delivery. Treatment under this program should at least be consistent with the Emergency Feed Assistance Program which allows reimbursement of transportation costs to the county line.

Limitations on cost sharing for well construction have also surprised many of our members. Producers who were forced to dig new wells when the drought dried up their supply of water for livestock, have also discovered to their chagrin, that they are not generally eligible for cost-share reimbursement under Section 607(b)(2) of the Emergency Livestock Feed Assistance Act of 1988. Reimbursement of costs in construction or deepening of wells for livestock water should not be limited to grazing situations only. Pork producers who demonstrate legitimate need should be eligible for this type of cost-share assistance.

We understand from ASCS that pork producers will have their eligibility for feed assistance for the current feeding period extended to the fall of 1989 when the next crop becomes available. Because hogs consume grain throughout the year and cannot make use of pasture in the spring, like other livestock, they should clearly be eligible for feed assistance through the fall of this year. But again we are concerned about the multi-species situation, where the farmer has a mix of hogs and cattle. We understand that ASCS will deny access to the feed programs through the 1989 fall crop harvest, where the farmer has excess hay or pasture and a few cattle. I can speak from personal experience that my hogs cannot live on pasture.

Let me say again that the Committee should be commended for its immediate reaction to farmers during the drought of 1988. Last year was certainly a tough time and all farmers need to understand the grave difficulties in striking a balance between various interests. We compliment the Committee for that effort.

However, it is unfortunate that the Livestock Programs Division of the ASCS continues to be unable to promulgate the final rules on the emergency feed regulations, although the legislation was passed by Congress some seven months ago. It's also unfortunate that the final regulations are not available, when the last day for application, under the feed programs, is March 31, 1989. Of course, we can resubmit applications for feed assistance after next week, but much of the confusion over the programs at the local level could have been avoided if the Livestock Division had been more diligent in getting the rule out. We do understand that a new handbook is coming out to assist with the emergency feed programs.

Pork producers can certainly sympathize with the overworked ASCS staff at the county level that must deal with these complex issues on a daily basis. We believe that much of the paperwork and guidelines required for the emergency feed programs are unnecessary, time consuming, and costly for the livestock producer and for ASCS alike. Moreover, the rules should be simplified, so all county offices handle the emergency feed programs the same way.

We realize that the Secretary of Agriculture has an extremely hectic schedule, but we believe that we need to at least have one of his representatives go to the country and visit firsthand with local ASC offices and livestock producers. After walking through the procedure to apply for feed assistance, it would be immediately obvious that the regulations and the attendant paperwork are unduly confusing and also unreasonable.

We ask that you investigate the Livestock Division's apparent lack of responsiveness and assess whether an extension of time for producers to apply for the emergency feed programs would be appropriate under the circumstances. We would also like to see an accounting of benefits distributed to livestock producers in 1988 and 1989. Quite frankly, I am concerned that producers have been unfairly turned away from potential feed benefits by reasons not intended by Congress.

The National Pork Producers Council offers its services to sort through the complexities of the feed assistance programs. We look forward to working with this Committee on other issues as they arise.

OUTLOOK FOR THE 1989 WHEAT CROP

THURSDAY, APRIL 6, 1989

House of Representatives,
Subcommittee on Wheat, Soybeans, and Feed Grains,
Committee on Agriculture,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 1302 Longworth House Office Building, Hon. Dan Glickman (chairman of the subcommittee) presiding.

Present: Representatives Johnson, English, Volkmer, Penny, Nagle, Sarpalius, Dyson, Marlenee, and Roberts.

Staff present: Fred J. Clark, associate counsel; Glenda L. Temple, clerk; Greg Frazier, James A. Davis, Howard Conley, Thomas H. Lederer, and Cliff Humphrey.

Mr. Glickman. Why do we not go ahead and begin. I think we will not have to face today repetitive bills. I do not believe there are votes today, as I best recall. So we ought to be able to finish this hearing by about 12 o'clock.

OPENING STATEMENT OF HON. DAN GLICKMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. Glickman. Last week I was in Kansas and I can confirm what we have all read in the newspapers and seen on the television over the last few weeks: We face the potential of a major shortfall in the 1989 Winter wheat harvest.

The drought which ravaged the Corn Belt last year has not been broken in the Great Plains. It is 12 months more severe, and in spite of the rains which have fallen in spots across the region, farmers in most of the State tell me that the damage is done to the crop. And just in the last 2 or 3 days, I have received several hundred calls from Kansas talking about damage between 30 and 75 percent in most cases, and today we will have some testimony on exactly how it is and how it appears to be in the future.

That damage presents the subcommittee with a set of serious problems which we will examine this morning. If rains do not come to the Winter Wheat Belt in sufficient quantities in the next few weeks to make an average harvest, given the fact that the United States is carrying historically low levels of wheat stocks, the situation will have enormous implications for domestic food prices and supply, our ability to supply the export market, and may mean the difference between whether some farmers are still on the land next year. And I may add parenthetically, in some cases, even if rains come in generous quantities, the damage has already been done.

Domestic food policy, budget policy, trade policies, and basic farm programs are all going to be affected by the weather, just as they were last year. I believe it is prudent for this subcommittee, working in cooperation with the full committee and the Department of Agriculture to begin making plans for this eventuality. It is easier to cancel at the last minute such a plan than to develop and implement a proposal to meet a serious challenge at the last minute.

While we need to prepare for the entire gamut of ramifications for a drought in Winter wheat country, I believe one of the first priorities of this subcommittee and committee is to address the concerns of the farmers who will suffer financial damage from a drought, in the same way we did when the drought hit the Corn Belt last year.

For my part, I would like to explore the following options as responses to the drought and ways to make sure that farmers receive assistance. I am going to present four options, not all of them will necessarily be what we come up with, but at least they are things which I think perhaps we ought to focus our remedies around.

One, an extension of the 1988 drought bill into 1989; two, modifying the 1988 drought bill to clarify that Winter wheat, because of the peculiar relationship of its growing year with calendar years, growers can receive aid under that bill; three, extending the enrollment period for 0/92 for 1989 crops for farmers along with modifications to the 0/92 program to ensure that under such an option farmers would be guaranteed the maximum statutory deficiency payments and not just the maximum projected deficiency payment; and four, extending the enrollment period for farmers to take Federal crop insurance protection for the 1989 Winter wheat crop, or thus opening the period to buy crop insurance for those producers.

Now these are four options that I think that we have to at least look at in connection with what we might be doing if legislation is necessary. These options are not exclusive of other possibilities and should be, I think, explored along with administrative actions the Secretary might take, such as, permitting haying and grazing and ensuring that applications for failed acreage determinations be made as quickly as possible.

Finally, in exploring these options, which I just mentioned, a process I hope can begin this morning during our discussion with the witnesses. I believe we need to remain mindful of the political and legislative parameters within which we will have to operate. I do not want to get into a situation which embroils this subcommittee and the full committee in an endless controversy about adding extraneous features to legislation to address the problem at hand, and I would also want to develop a bill which can be passed by the Congress, which means it has to be sensitive to the boundaries imposed by the budget.

I would also hope that knowing the situation and the subcommittee's concern with the problem, that the Secretary will be prevailed upon to exercise his enormous discretionary authority he has at his disposal to help solve many of the problems in the Great Plains, much of which if done, would obviate the need for additional Federal legislation.

Before yielding to the other members for their opening comments, I want to welcome all of our witnesses who are here. I think we have the kind of witnesses that will be able to tell us generally what our problems are and what the best way is to solve them. So before I begin, however, I would like to yield to the ranking minority member of this subcommittee, my colleague from Montana, Mr. Marlenee.

OPENING STATEMENT OF HON. RON MARLENEE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MONTANA

Mr. MARLENEE. Thank you, Mr. Chairman. I commend you for having what may become one of the focal points of the Agriculture Committee if not the full Congress in Washington, D.C. here, and congratulate you on some well thought out points and your presentation, Mr. Chairman. I stand ready to work with you as I always have been in the past, stand ready to work with you in case there is an instant replay of last year's drought.

I have learned to become somewhat pessimistic or cautiously pessimistic, I guess I should say with regard to Mother Nature when we are dealing with agriculture. In one way it certainly benefits us and in another way it benefits us by having the diminishing surplus. But it certainly does so at the expense of the agriculture producer.

I would remind the committee and the general public at large that the disaster bill of last year cost us very little money and when you take into consideration the fact that we saved enough money under the Deficiency Payment Program and under the Export Enhancement Program, we saved enough money to more than fund the Disaster Program that we had. We do have available to us the Federal Crop Insurance Program, but at best this is an ineffective tool to deal with the kind of droughts that we have had in the past and we still need to evaluate that program, to strengthen that Crop Insurance Program because of the red tape and continuing droughts in some areas and particularly if there are replays, it is almost worthless with regard to protecting the investments an agricultural producer makes in his production in order to bring food to the table of the American public.

And with that, Mr. Chairman, I yield back the balance of my time.

[The prepared statement of Mr. Marlenee follows:]

Statement by the Hon. Ron Marlenee
Subcommittee on Wheat, Soybeans & Feed Grains
House Committee on Agriculture
Thursday, April 6, 1989

Mr. Chairman,

I thank you for recognizing me and I join in welcoming our witnesses before the panel today.

I am also concerned about the continuing outlook for another disaster year for several parts of our country. While we all hope and pray that conditions will improve, as a farmer myself I have learned over the years to be **cautiously pessimistic** much of the time when it comes to depending on Mother Nature to make the crop.

Members of this subcommittee and of the full committee should know that I will certainly work with our Chairman and with them to again help provide whatever assistance may prove necessary in the event of an "instant replay" of last year's disaster. There is no good reason why the 1988 Disaster Assistance Act could not be extended to cover 1989 crops which are lost to drought or other natural disasters, and I certainly agree with the Gentleman from Kansas with regard to applying the 1988 Act to winter wheat which was seeded -- much of it in scorched, dusty fields -- in 1988, and was due to be harvested this spring. In much of the winter wheat area the drought has not been broken, and our farmers will face yet another bleak harvest.

I note that the Chairman has listed among his options a suggestion that we might allow late sign-up for crop insurance. I would simply note again for the record that at the present time Federal crop insurance is a practically worthless tool for most producers in this country. At best a producer can **maybe** hope to recover somewhere between 1/2 to 3/4 of his actual outlays which were incurred in preparing and seeding his fields **if . . . and I emphasize "IF" . . .** he has taken out the highest coverage provided under the current program. This still leaves him with an absolute loss on his 1989 operating financing, and zero profits with which to meet his family's needs and pay other long-term debt.

With these brief remarks, I will yield the balance of my time and look forward to hearing from our witnesses.

Mr. **Glickman**. Thank you, Mr. Marlenee. I may also mention before I recognize Mr. Johnson. The Department has answered, for the record, in response to my questions of the last hearing, and I would like those to be made part of the record. I want to make sure all the members have copies of that. It has to do with the costs of the program. I will make sure you get it.

But it will be relevant to the questions we ask Mr. Wilson and I want to make sure we get it before we start the questions because the Department talks about what will happen to the cost to the programs in the event the weather conditions continue and how much we save for every nickel of deficiency payment that is not paid. These are relevant facts in terms of how much we have to spend.

[The information follows:]

QUESTIONS FROM THE HEARING MARCH 23, 1989
SUBCOMMITTEE ON WHEAT, SOYBEANS, AND FEED GRAINS
COMMITTEE ON AGRICULTURE

Questions for the record from Chairman Glickman:

1. What are USDA's projections for wheat program costs for the 1989 crop if current weather conditions do not improve to at least normal and average?

Answer: The President's Budget presentation to Congress on February 9, 1989, estimated deficiency payments for the 1989 crop of wheat to be about $1 billion. The forecast was made as of late November, with a projected wheat farm price of $3.60 a bushel and expected yields slightly below trend. Estimates have not been updated since that time. However, based on conditions that have developed since late November, crop prospects, especially in Kansas, have deteriorated. As a result, our production prospects are likely somewhat lower and price expectations are higher. This would suggest program costs below $1 billion at this time.

2. How will those projections compare to the present OMB baseline for spending associated with the 1989 winter wheat crop?

Answer: With poor weather conditions for the winter wheat crop it appears that yields could be lower than expected, resulting in higher farm prices and lower deficiency payments. For every 5 cent per bushel decrease in the deficiency payment rate, deficiency payments will decrease by about $100 million.

3. Is USDA presently evaluating options in the event present weather conditions do not improve and if so, what options are under consideration?

Answer: Since the 1930's, we have experienced only four droughts of the magnitude of the one last year. We have never witnessed back-to-back severe droughts. In fact, over the last 20 years, yields of major crops have rebounded to within 10 percent of "normal" following severe droughts, such as in 1980 and 1983.

Nevertheless, USDA meteorologists are carefully monitoring the weather situation across the United states and briefings are being presented on a regular basis to top USDA staff. In addition, weather briefings are being made to Members of the Congress. Also, on a technical level, monthly meetings of the Interagency Drought Task Force are being held to assess the current situation and advise top officials.

Options are limited for changes in the 1989 Wheat Program. Winter wheat is planted and the planting of spring wheat is approaching. The Department is in the process of evaluating alternative program parameters for the 1990 crop in light of the weather problems associated with the 1989 crop.

4. Is USDA prepared to approve state requests for year-long haying and grazing of idled wheat acreage on an expedited basis?

Answer: Procedure is being developed to handle the State requests similar to that of 1988. The county ASCS office will telemail the required information pertaining to the disaster and the need for emergency haying and grazing of the idled wheat acreage to the State ASCS office. After concurrence by the State ASCS office, the county request will be FAXED into the Deputy Administrator, State and County Operations. We are prepared to provide a turn-around time of less than 24 hours following receipt of the request. The decision will be telephoned to the State ASCS office, who shall immediately telephone the county ASCS office. The county ASCS office shall then use the fastest means available to notify the producers in the county.

5. Is USDA prepared to make an expedited decision with respect to failed acreage requests to ensure farmers have options on their 1989 wheat acres?

Answer: Standard operating procedure is in place for the handling of failed acreage requests. Requests for failed acreage must be filed within 15 days after the disaster occurs, but before all evidence of the crop is destroyed. However, county ASC committees must be satisfied that the cause of the failure was indeed a condition beyond the producer's control and that the crop was affected to the extent that it would be uneconomical to harvest.

Mr. **Glickman**. Now, Mr. Johnson.

OPENING STATEMENT OF HON. TIM JOHNSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF SOUTH DAKOTA

Mr. **Johnson**. Thank you, Mr. Chairman. I commend you as well for holding this hearing. I am looking forward to listening to the testimony relative to the weather outlook, the outlook for the winter wheat crop generally and implications for the 1990 wheat program, wheat exports and wheat stocks. The precipitation situation in the Northern Plains of South Dakota has improved somewhat, however, it is still spotty.

We still have a great number of concerns about the possibility of planting Spring wheat on failed Winter wheat acreage and obviously what happens in Kansas, a State that produces about one-fourth of the Nation's Winter wheat crop has serious implications for wheat growers generally.

I am looking forward as well to continued examination and analysis of the proposals that you have suggested and looking to see how we can fit some sort of concrete affirmative action within the context of a very difficult agricultural budget. So thank you, Mr. Chairman, and I have no further statements.

Mr. **Glickman**. Thank you. My colleague from Kansas, Mr. Roberts.

OPENING STATEMENT OF HON. PAT ROBERTS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. **Roberts**. Thank you, Mr. Chairman. I want to thank you also for calling this hearing. I would like to associate myself with your remarks. I want to thank my colleague from Montana for his leadership in regard to the situation that is being faeed by Winter wheat producers.

Since the hearing on March [illegible]3, Kansas has been blessed with some rain. Not enough rain, just a little portion. The good news is that these rains have helped ease the blowing conditions that made the front pages of all of the newspapers in mid-March. The bad news is that Kansas wheat—and we grow more wheat in my district than any other State—does remain in very very critical condition.

The most recent Wheat Quality Council report notes that 75 percent of the Kansas wheat crop, and I must say to my colleague from Oklahoma, I know he is experiencing the same kind of difficulty, the same thing up in Nebraska, the same thing in eastern Colorado, is rated at poor to very poor. More to the point, the damage is not isolated to specific areas. The field inspections show nearly every farmer will face some yield and quality in regard to their reduction problems. The key questions will be to what extent.

In our previous hearing, I discussed four options. They more or less parallel the options that were discussed by the chairman. I have shared these with Secretary Yeutter, and with the administration. In a personal meeting with him, we went over those suggestions and the process has begun. The Kansas ASCS office, and I think some other States as well, has requested emergency haying and grazing which will help ease the concerns in regard to forage.

The producers indicate information relative to filing for failed acreage designation is readily available in local ASCS offices not as soon as I would have liked them. And we still have some problems with the Federal Crop folks in regard to what you have to do, but it seems that we are always faced with those problems.

I think these first steps have helped reduce the blood pressure for farmers who are really coping with a very bleak outlook for Winter wheat. And I urge the Department to continue their efforts as more information becomes available on the extent of the damage.

We are talking a basic legislative contingency plan here. Over the past few weeks in working with my colleagues, and more especially the chairman, we have examined several policy options. And I believe an assistance package for Winter wheat producers should and must be consistent with the carefully drafted legislation that resulted in the Disaster Assistance Act of 1988.

And to that end, I have drafted what I refer to as a technical amendment. A technical and conforming amendment, if you will, to the 1988 act which will extend the yield reduction assistance under title II to cover the 1989 Winter wheat crop. I have the bill in my hand. I am going to introduce it at 11 when we go into discussion. This approach does reduce or eliminate some of the problems with the administration of such a program by relying on regs and procedures already in place. You said during that bill last time, many of my colleagues, this was a blueprint. It was a foundation from which we could build. And I think the producers are very familiar with the act's procedures and thereby it would reduce their management burdens at a very critical time.

In addition, I want to assure my colleagues, this is not simply an issue bill. We do not need an issue in my country; we need assistance. I have included language to extend the act's requirement of multiperil crop insurance coverage for Winter wheat yield losses exceeding 65 percent.

My frustrations and concerns with multiperil crop insurance problems faced by Kansas producers are well known. Mr. English and myself have had very similar concerns and we have made them well known. Rest assured, I still have those frustrations. And the commission that is now set up is holding hearings all across the country. I hope we can get some answers.

But I recognize that if the FCIC program is to have a chance of really correcting all of these problem areas and improving its position in the minds of our High Plains producers, it must not be undermined by Federal disaster assistance. I know that.

Mr. Chairman, before I yield back, I want to reiterate this is a contingency package. Kansas producers have suffered very significant losses and it does spread into other States. Early estimates suggest 100 million bushels less than last year.

Some believe that it is too early in the process to make hard and fast decisions, and the chairman has indicated we do not want endless controversy. I do not want endless dry conditions and for us to talk while the producer needs assistance. It is not too early to begin addressing the producers' concern in a responsible and common sense manner. I will introduce the bill today. If we have a vehicle with which we can work, we can start the mark-up procedure when the chairman indicates with the understanding and agreement of the full Ag Committee, but I think it is time to move.

I would say one other thing. I want to go back to the discussion of last year's Disaster Act. There was considerable discussion that this, in fact, was a blueprint, was a foundation from which we could move. And corn country went through a lot of trauma and pain and suffering last year and this Congress responded.

I am not going to get into the political situation or the fact that we had some deficiency payment savings with which to work. As of this year, we do not have that political situation and the budget situation is very severe. But we are talking about a significant reduction of our Winter wheat supply, and if the Disaster Assistance Program and its intent means anything, it should address this problem. The farmers will not be made whole, if they have Federal crop, if they have the disaster assistance, they can be made partially whole.

It seems to me that this kind of a technical amendment is in good keeping and in faith with that disaster bill. More to the point, this is my district. It is my people. We are suffering. We were able to work with corn country last year. It is our time. I thank the Chairman.

[The prepared statement of Mr. Roberts follows:]

The Honorable Pat Roberts
Wheat, Soybeans and Feed Grains Subcommittee
April 6, 1989

OUTLOOK FOR THE 1989 WHEAT CROP; RELATED ISSUES

Mr. Chairman, thank you for calling this hearing. I also want to thank my colleague from Montana, Mr. Marlenee, for his leadership relative to the situation faced by winter wheat producers.

Since our drought-related hearing on March 23, Kansas has been blessed with some precipitation. The good news is the rains have helped ease the blowing conditions prevalent in mid March. The bad news is Kansas wheat remains in critical condition.

The most recent Wheat Quality Council report notes that 75 percent of the Kansas wheat crop is rated at poor to very poor. More to the point, the damage is not isolated to specific areas. Field inspections show nearly every farmer will face some yield and quality reduction problems -- the key question will be to what extent.

In our previous hearing, I discussed four administrative options I'd shared with Secretary Yeutter. I understand the process has begun with regard to those suggestions.

-- The Kansas ASCS office has requested emergency haying and grazing which will help ease forage concerns.

-- Producers indicate information relative to filing for failed acreage designations is readily available in local ASCS offices.

These important first steps have helped reduce the blood pressure for farmers coping with the bleak outlook for winter wheat. I again urge the Department to continue their efforts as more information becomes available on the extent of the damage.

Today, I want to discuss a basic legislative contingency plan. Over the past few weeks, I've examined several policy options to help producers cope with the drought situation.

I believe an assistance package for winter wheat producers should -- must -- be consistent with the carefully crafted legislation that resulted in the Disaster Assistance Act of 1988.

To that end, I've drafted a technical amendment to the 1988 Act which will extend the yield reduction assistance under Title Two to cover the 1989 winter wheat crop.

This approach reduces or eliminates administrative problems by relying on regulations and procedures already in place. And, producers are familiar with the Act's procedures, reducing their management burdens at a critical time.

In addition, to assure my colleagues this is not simply an "issue" bill, I've included language to extend the Act's requirement of multi-peril crop insurance coverage for winter wheat yield losses exceeding 65 percent.

My frustrations and concerns with multi-peril crop insurance problems faced by Kansas producers are well known. Rest assured, those frustrations still exist.

However, even I recognize that if the FCIC program is to have a chance of correcting its problem areas and improving its position in the minds of High Plains producers, it must not be undermined by federal disaster assistance.

Mr. Chairman, before I yield back, I want to reiterate this is a contingency package. Kansas producers have suffered significant losses -- early estimates suggest 100 million bushels less than last year. (NOTE: your projected 65 percent harvest factored into last year's 323 million bushels equals about 210 million bushels.)

Some believe it is still too early in the process to make hard and fast decisions. However, it is not too early to begin addressing producers' concern in a responsible, common sense manner.

I thank the Subcommittee and look forward to hearing our witnesses comments and observations.

Mr. **Glickman**. Thank you, Mr. Roberts. Now the chairman of the Subcommittee on Conservation, Credit, and Rural Development, Mr. English.

OPENING STATEMENT OF HON. GLENN ENGLISH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OKLAHOMA

Mr. **English**. Thank you very much, Mr. Chairman. As Mr. Roberts pointed out, I think he has the largest wheat producing district in this Nation. By most accounts, my district, western Oklahoma is the second largest. I have found many of the same problems that he has pointed to and the chairman has indicated.

Out in my district this last week, the discussions that we were having with farmers and from what I could see personally, we have a real disaster. There is no question that the rain is not going to restore that crop. It is not going to make that crop. I do not care if you put it 5 feet under water, it is not going to restore that crop. That is the reality that we are looking at. It is gone.

It has been estimated that in my district roughly 20 percent of the crop is lost. There will be areas in which we will see a greening of what is left of that crop. That does not mean that it is going to make grain, that it is going to produce, and that is another point that I think may be deceiving with some people. As these rains come across parts of Oklahoma and Kansas, there will be some greening taking place and lead many people to believe that that crop can be in some way be restored. But it is too late. The grain-producing ability has already been lost and I think that that has to be recognized.

With regard to the question of crop insurance. Our Subcommittee on Conservation, Credit, and Rural Development has already announced on September 1, we will begin revamping of the Crop Insurance Program. The problem is that that revamping will not quite take place in time to deal with this problem. It will be a part of the Farm Program. We certainly intend to make the Crop Insurance Program work, but I think we all recognize that there are serious deficiencies with that program at this time.

And with that in mind I think fairness dictates, fairness requires that this Congress pass legislation similar to what was passed last year for those producers in the mid-West when they faced a similar situation. Also though, I think, that we have got to recognize that there had been some problems with that 1988 disaster bill. And that is particularly true with regard to the application of that legislation.

We are finding differences between the application in the different States. We are even finding differences between counties. And there has to be some uniformity brought to bear, I think, if this legislation is going to be provided and I would certainly hope the Department of Agriculture would make an effort to maintain consistency across State lines and across county lines to make sure that farmers are treated alike no matter what county or what area they live in.

I think it should also be understood that under these circumstances the people who are affected are in fact facing genuine disasters. Genuine disasters mean many of these people, unless they do receive assistance, simply will not be in business. It means many of the people who depend upon those farmers, I am talking about the small merchants in the communities and the area and even in the States, even some of the metropolitan areas in these States are going to feel this economic blow.

So I think as I said when the call is sent forth from the mid-West last year, this committee, this subcommittee responded, as did the Congress, and as did the President. And certainly those of us who assisted in that effort, who supported that effort are now requesting the same treatment for our districts and our States. And I certainly want to commend the chairman for holding these hearings. Thank you, Mr. Chairman.

Mr. GLICKMAN. Thank you, Mr. English.

Mr. Dyson.

OPENING STATEMENT OF HON. ROY DYSON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MARYLAND

Mr. DYSON. Thank you, Mr. Chairman. I just have a brief statement. In the State of Maryland, our Winter wheat crop is about $16.7 million. I guess this is not much compared to your $1 billion market in Kansas. Therefore, my personal concern today is for the Maryland consumer. The State of Kansas contributes about one-sixth of the total U.S.-wheat harvest.

Clearly, if a quarter of the Kansas Winter wheat crop may be destroyed this year, it is going to have an impact on people who shop in Maryland. I congratulate you on having this hearing today. I am prepared to support measures which will assist our drought-stricken Kansas farmers.

Mr. GLICKMAN. Thank you, Mr. Dyson.

Mr. English.

Mr. ENGLISH. One point, the staff just handed me. We have compiled the percentages in the various States that are affected by this drought of crop insurance. I thought that might be helpful for the record, and I would ask that staff could hand that out. It indicates, for instance, Colorado, 33 percent has crop insurance. So that crop is handled by crop insurance. Kansas, 41 percent. Nebraska, 51 percent. Texas, 28 percent. Oklahoma, 17 percent. So we are extremely supportive of this disaster legislation or any disaster legislation that might be considered, Mr. Chairman.

[The information follows:]

winter wheat state--1989 crop year
per FCIC 3/2/89 rept., and EEG 3/? advice:

(000,000)	ACRES	TOTAL	NASS PLANTED (1988)(%)
Colorado:			
FCIC:	.127		
RC:	.729		
		.906	2.7 (33.6)
Kansas:			
FCIC:	.239		
RC:	3.939		
		4.178	10.2 (41.)
Nebraska:			
FCIC:	.215		
RC:	.966		
		1.181	2.3 (51.4)
Oklahoma:			
FCIC:	.295		
RC:	.917		
		1.212	7.0 (17.3)
Texas:			
FCIC:	.223		
RC:	1.575		
		1.798	6.3 (28.5)

Mr. GLICKMAN. Thank you. That will be made part of the record. Dr. Wilson, it is a pleasure to have you here. I think you are accompanied by Dr. Strommen, your Chief Meteorologist, but I am going to let you proceed. But I would like both of you to testify essentially at the same time, so we can ask questions of both of you.

STATEMENT OF EWEN M. WILSON, ASSISTANT SECRETARY FOR ECONOMICS, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY NORTON STROMMEN, CHIEF METEOROLOGIST; KEITH COLLINS, DIRECTOR, ECONOMIC ANALYSIS STAFF; AND LEO MAYER, DEPUTY ASSISTANT SECRETARY FOR ECONOMICS

Mr. WILSON. Thank you, Mr. Chairman. Dr. Strommen is here today and also Dr. Keith Collins who is Director of my Economic Analysis Staff.

Mr. GLICKMAN. Maybe all three of them could come up here, so that you would not have to turn your head around.

Mr. WILSON. I would also mention that my deputy Dr. Leo Mayer is here. He is a Kansas boy. He was born on a farm in Clyde, Kansas, and grew up there. He was out there this weekend and he brought some pictures back which have given me some sense of the magnitude of this problem. Leo took a trip from Oklahoma City up through the western part of Kansas and then across the north to Manhattan down through Wichita and out of Wichita and there is some interesting——

Mr. GLICKMAN. Could you pass some of the pictures around too, so that we could take a look at them, as well?

Mr. WILSON. Certainly. With your permission, Mr. Chairman, I will read a brief statement and then we will respond to your questions. In your letter inviting us up to this hearing you asked us to discuss, first of all the weather outlook; second, the outlook for the Winter wheat crop; and third implications for the 1990 wheat program, wheat exports and stocks.

Let me start with a brief comment about the weather. Precipitation this year has been above average in the northern Great Plains, in much of Colorado, and in a broad belt of the country extending from the Ohio River Valley to the southern Mississippi Delta. On the other hand much of western Kansas, eastern Colorado, the Oklahoma/Texas Panhandle, and southern Nebraska have had below average precipitation.

Kansas normally receives about 6 inches of precipitation in the months of October through February. Typically, 2.1 inches fall in October, 1.3 inches in November, 0.9 of an inch in December, 0.7 of an inch in January, and 0.9 in February. This year only 3 inches of precipitation were recorded for all of these months, and this combined with great swings in temperatures have stressed the crop in much of Kansas.

Kansas does normally get good spring rains: 1.8 inches in March, 2.5 inches in April, 4 inches in May, and 4.1 inches in June. In March of this year, precipitation totaled about 1.3 inches. Therefore, good rain in April and May will be critical for development of the Hard Winter wheat crop in Kansas.

The long-term Palmer Index which measures prolonged and abnormal moisture deficiency or excess, shows that pockets of drought persist from last summer in parts of the western Corn Belt, in parts of the Northern Plains, in parts of the far West, and in southeast Texas. Good spring rains will be needed for crop developments in these areas. On the other hands, subsoil moisture has been fully recharged in much of the Soft Red Winter wheat area extending from the eastern Corn Belt through the Southeast.

The wheat outlook in the area of Kansas which received less than 50 percent of normal precipitation from October through February produced about 85 percent of the Kansas wheat crop last year. In a normal year, Kansas accounts for about 35 percent of the Nation's Hard Red Winter wheat. Kansas normally accounts for 23 percent of all Winter wheat and about 17 percent of the total wheat crop, including Spring wheat and Durum.

The dryness has caused deterioration of the Winter wheat crop from Kansas southward into northern Texas. In addition, sharply fluctuating temperatures in early February may have caused well above-average winterkill. The only good news is that those cold outbreaks did eliminate many of the insects that had multiplied in the mild, winter weather. But there is no doubt that this dryness has caused much below-average tillering in wheat plants in western Kansas.

Not all of the Winter wheat crop has been affected by drought. Near to above-normal amounts of winter precipitation in much of Texas, Oklahoma, parts of Nebraska, and Colorado have provided more favorable conditions for crop development in those areas. This is also true in the Soft Red Winter wheat areas. Precipitation was favorable across the Delta, from southern Missouri into Ohio, and rains were timely in the Southeast during the critical tillering stage.

In most of the White wheat winter areas of Michigan and the Pacific Northwest precipitation has been adequate to abundant. The Hard Red Winter wheat areas in the northern Great Plains which is mostly a spring wheat area, have benefited from good snow cover during the winter season, but subsoil moisture reserves remain below normal and more rain will be needed for a recharge of those areas.

The key to the 1989 crop will be the timing, the amount and the distribution of spring rainfall. At this early stage, the only indication we have of crop conditions is provided by the weekly reports of the Department's National Agricultural Statistical Service. I do have some detail on that in my written statements, but to summarize what those numbers are telling us: crop conditions this year, especially in Kansas, is far worse than 1 year ago. But we have seen an improvement in the readings between March 27 and April 3. We got some rainfall during that period.

Another indication of what is going on is in some satellite photos. Now normally we start buying satellite images from the Landsat satellite starting April 1. These images are from the polar-orbiting weather satellite and they do not have quite the same resolution as in the Landsat but these images were as of the third week of March 1988 and third week of March 1989.

The key to analyzing those pictures is that red indicates vegetative cover. And as you take a look at those pictures, I think you can see that in 1989, there is far less red than there was in 1988.

When we start getting pictures later in the season from Landsat, we will have some indication of whether that situation improves.

The overall condition of the Kansas crop was rated at 61 percent of normal on April 3. And recent history indicates that the overall crop conditions of poor to very poor on April 1 result in yields that are below trend, but the yield loss—the exact yield loss is quite uncertain. Just to give you an example, the Kansas wheat crop back in April 1, 1977, was rated at 67 percent of normal and yields turned out to be 5 bushels below the trend line. On the other hand, in April 1957, the condition of the Kansas wheat was reported at 60 percent of normal, but that year yields ended up 4 bushels above trend. It turned out that above normal rainfall in March through May saved the crop.

Based on Kansas precipitation data for the period October through February, this season is the fifth driest in records going back to 1931. Records show that in 7 of the 10 driest seasons since 1931, Kansas wheat yields have been below trend.

The 1990 wheat program. The public comment period for the 1990 wheat program started last week. Three levels of acreage reduction are considered in USDA's preliminary regulatory impact analysis: 10 percent, 5 percent, and zero percent. It is assumed that 11.5 million base acres of wheat will be enrolled in the long-term Conservation Reserve Program by 1990. The target price is assumed to be $4 a bushel; the loan rate $1.95 a bushel, both of which are the minimum levels established by law. This compares with a target price of $4.10 a bushel this year, and a loan rate of $2.06 a bushel this year.

Based on preliminary analysis, the difference between a zero percent ARP and a 10 percent ARP is 175 million bushels of production, 75 million bushels of exports, and 75 million bushels of ending stocks. But these estimates should be viewed with caution. There is still a great deal of uncertainty associated with estimates of the 1990 crop supply and demand situation when we do not have a good estimate yet of the 1989 wheat crop.

Back in January, USDA estimated that wheat farmers seeded 54.5 million acres of Winter wheat. Last Friday, we published prospective plantings on wheat based on a survey conducted between March 1 and March 15. It appears now that the Winter wheat acreage will total 54.7 million acres. That is up 12 percent from 1 year ago. Durum wheat acreage was put at 3.9 million acres, up 16 percent from 1988, and other Spring wheat, 15.7 million acres, up 17 percent from last year. When you add this up, total wheat acreage this year is estimated at 74.3 million acres, up 13 percent from 1 year ago.

USDA will issue its first assessment of the 1989 wheat crop on May 11, but Mr. Chairman, you did ask us to provide an estimate of the wheat crop today, if adverse weathers continue. If yields for Kansas decline from trend by an amount equal to the largest decline ever—that would be 10 bushels an acre—and if 19 percent of planted acres are abandoned this year—that would be the worst rate of abandonment in 20 years—then Kansas wheat production could fall to 280 million bushels. That would be about 150 million bushels below the level that could be achieved under normal conditions. If you allow for some additional loss in surrounding States, this implies a 1989 wheat crop of 2.3 billion bushels. I must emphasize that this is not an official USDA projection. You will have to wait until May 11 for that, but I think it does provide some perspective on the situation if dry conditions persist.

If the 1989 wheat crop is only 2.3 billion bushels, ending stocks on June 1 1990, likely would fall below 500 million bushels. Exports also would be down, perhaps below 1.4 billion bushels compared with 1.5 billion bushels in the current marketing year. Under these circumstances, the lower acreage reduction options for the 1990 crop became more plausible.

Since the 1990 program does not have to be announced until June 1, there is still 2 months in which to evaluate crop and weather developments before making that acreage reduction decision. As you know, any acreage reduction decision announced by June 1, could still be modified up until July 31, if supply and demand conditions warrant such a change.

At the present time, prospects for the Soft Red Winter wheat crop appear very favorable, especially in the eastern Corn Belt and the Southeast. Planting conditions in the Northern Plains are generally favorable for Spring wheat and Durum. But by June 1, we will certainly know much more about the potential size of the 1989 wheat crop and we will be in a better position to choose the appropriate acreage reduction level, if any.

That concludes my testimony, and I will do my best to respond to questions that you or other members may have, Mr. Chairman.

[The prepared statement of Mr. Wilson appears at the conclusion of the hearing.]

Mr. GLICKMAN. I would if we might ask Dr. Strommen now—you did give the committee kind of an informal briefing when Chairman de la Garza was there, but I think it would be worthwhile. I know you have some charts that are attached to Dr. Wilson's testimony, but I think it would be a good point for you to give us the current weather situation and what projections you see.

OPENING STATEMENT OF NORTON STROMMEN, CHIEF METEOROLOGIST, U.S. DEPARTMENT OF AGRICULTURE

Mr. STROMMEN. Thank you, Mr. Chairman. This last week we did get some very excellent moisture over parts of the Winter Wheat Belt. This will be highly beneficial to those areas which received that moisture. However, we have some other areas—I am just looking at the latest summary for March and when you look at that, you find that much of Oklahoma, southeastern Kansas, and the Soft Red Winter Wheat Belt, the Southeast all got excellent moisture during the month of March, as did the Pacific Northwest. So these areas got excellent moisture.

The area of deficit in March extended across Iowa, Nebraska, western Kansas, eastern Colorado, and the Texas/Oklahoma panhandles, where amounts were generally less than one-half an inch, and this continues to put stress on that crop. I think the combination of the very severe cold outbreak in February, combined with the dryness is now becoming apparent in all of these surveys that have been taken in these Western areas.

In looking at the historical records, it has indicated that we can get some recovery, but in some of these areas there simply are no plants left. And those are losses which we cannot recover at this point. I would simply say that because we have very limited subsoil moisture that the development of this year's crop is going to be strictly dependent on the timing, distribution and amount of rainfall this spring is more critical than ever.

Now when we look at the National Weather Service 30-day outlook which was just released this week, it suggests that we will still have below normal rainfall during the next 30 days for major portions of the Great Plains Winter Wheat Belt. However, the crop is also experiencing cooler than normal temperatures which means that it will be later in its development. When you look at the 90-day outlook from the National Weather Service, it suggests we will return to a distribution which is more near normal during that period.

By delaying the development of the crop, that gives us a better chance to get more response to the more favorable conditions which have been suggested in the outlook beyond the first 30 days, so that we have a mixed picture.

I think that at this time, we can say that, yes, there is some crop losses that are unrecoverable. We also have to say that the final outcome is going to depend on what happens in the next 30 to 60 days by and large. And therefore, it is just a little premature to start to write the crop down to any specific level. We will simply have to watch and wait for the development and timing and distribution of the rainfall in the next 2 months.

So I think that is really the problem that we are looking at. Now I might add to that. Because we have had very little recharge of the aquifer, the water tables, in the past 24 months in the Great Plains, one of the other major problems that we need to be concerned about is the drying up of additional wells, particularly the shallow wells. This will be a problem that we will also have to be looking at, as well as the impact on crops.

Mr. **GLICKMAN**. If we may begin with questions now. I would like to ask, first of all, do you have any estimate of what percentage of the plants are left with no recovery possible. That is, I am trying to get a figure of even if you have generous rainfall or the kind of rainfall that the National Weather Service projects: lower than average the next 30 days, average the next 90 days, where are we left. Either Dr. Wilson or Dr. Strommen in terms of percentage of the crop gone, notwithstanding what happens?

Mr. **WILSON**. Mr. Chairman, in all honesty, I just do not think we have a good estimate of that right now. We are seeing in some areas crop that was in very bad shape a couple of weeks ago apparently making some sort of recovery. So it is just very difficult to get a firm estimate on that. We did have someone from our National Agricultural Statistics Service who was on the Kansas wheat tour a couple of weeks ago and he briefed me and he was unable to give me any firm estimate of that.

Mr. **GLICKMAN**. Anybody else can comment on that? Dr. Collins.

Mr. **COLLINS**. I might add that we will have a first survey of the abandonment of winter wheat on May 1, and that would be published in our May 11 report, and that would be the first hard numbers that we would have on percentage of acres that would not be harvested.

Mr. GLICKMAN. Second line of questions has to do with cost associated with a drought. In your answers to questions from me that you provided to this committee, and we appreciate that, you indicate that it is likely that the previously projected wheat farm price of $3.60 a bushel for the 1989 crop may be slightly low and that your expected yields may be below what you had projected them to be originally. And you indicate at the bottom, as a result our production prospects, are likely somewhat lower and price expectations are higher. This would suggest program costs below $1 billion at this time.

Hypothetically, if you had the loss, the maximum loss which you projected, let us say, for a crop of 2.3 billion bushels which in Kansas would be down about 150 million bushels, but you have got a loss in Oklahoma, we would suffer most of the loss. But there would be losses in Colorado, Nebraska, Oklahoma and Texas, as well. What would the savings of the program be on that loss vis-a-vis what you would project it to be?

Mr. WILSON. If we had that kind of loss, and just for the record, I want to say that 150 million bushel loss in Kansas is relative to a normal size crop. Back in 1988, we had a crop of about 330. I would hate anyone to interpret the crop reduction from that number. It is the crop reduction from something in excess of 400——

Mr. GLICKMAN. We understand that all your numbers are hypothetical. This is not an official number.

Mr. WILSON. If that happened and we got a 2.3 billion national crop then it seems to me that the price projected for the President's budget of $3.60 would certainly be low. It is conceivable that we could see a price somewhere in the range of $3.70 to $3.80. Every 5-cent reduction in deficiency payments that is implied by a higher price would save us in deficiency payments something like $100 million. So you are getting into the hundreds of millions of dollars difference here.

Mr. GLICKMAN. So hypothetically, if you had the full loss and if the price were 20 cents a bushel higher, again hypothetically you are talking about as much as $400 million in savings from deficiency payments. Now would there be any other savings or other additional costs?

Mr. WILSON. You may get some additional savings from repayment of loans which would be on top of that.

Mr. GLICKMAN. What would happen if you went, which I expect you probably will do, to a zero ARP or a 5 percent ARP? My judgment is that is the way you all are leaning would be my guess; how does that affect this?

Mr. WILSON. Mr. Chairman, I think it is too early to really say that. We have 2 months before we make that decision and then another 2 months before we lock it in.

Mr. GLICKMAN. So you do not like the way I was leading you into a closet when I could slam the door and trap you; right? That is assuming you went to a zero ARP. Would there be any savings or costs associated with that, that might affect these numbers? Obviously a zero ARP means more production, so less price.

Mr. **Wilson**. Well, you see at that point, you are talking about a zero ARP for the 1990 crop which is going to be reflected in the 1991 fiscal year. We have not even started talking about that. Not for the 1990 fiscal year or the current fiscal year.

Mr. **Glickman**. This goes a little bit to my first question. How much can we improve with quality spring rains. Dr. Strommen talked about the fact that a crop that looked really bad greened up and improved quite a bit. In the same way that I asked you what percentage of the crop is gone dead, unsalvageable; do you have any kind of way to quantify how much improvement there would be with the general quality spring rains?

Mr. **Strommen**. I do not think you can quantify it at this stage in the crop's development. Even though you get less tillering and some people have estimated that is down 15 to 20 percent, you could still get bigger heads and fuller heads which would add to that yield so that you can make up part of that loss. Therefore, you really cannot quantify it at this stage in the crop development. Those parts that you can quantify plant loss and there are unofficial estimates of a 15- to 20-percent winterkill across that area. Those plants are lost, but even that does not necessarily mean you lost 15 to 20 percent of the yield because of the response of the other plants that are still there, they can produce a bigger head and fuller kernels, and make up part of that loss.

So that is why it is very difficult at this stage of the crop's development to begin to quantify that final yield estimate.

Mr. **Glickman**. In addition, we are talking about Winter wheat now, you mentioned there were other areas of the country that still had some drought dry weather conditions. What other crops are materially effected by this besides Winter wheat. That is, if we come in with a disaster bill along the lines of what Mr. Roberts has talked about which is extending the program, we could extend it across the board for all crops or we could do it, as I put in my number two option, extend it for Winter wheat that was produced last year. Where else are we talking about in terms of potential effect?

Mr. **Strommen**. If you look at the overall soil moisture recharge during the winter, it has been extremely good in much of the eastern Corn Belt. There are pockets in the western Corn Belt which we only have moisture in the top part of the soil profile. This is areas that grow sorghum, soybeans, and corn. It also extends into some areas that grow sugar beets, some that have sunflowers.

Our situation as we go into the 1989 growing season is that we have generally enough moisture in the top part of the profile to germinate and establish the crop. That means that we have to have a continuation of appropriate summer rains in order to maintain the yield potential of that crop. There rains are necessary because we simply do not have, in the central and western Corn Belt, the deep soil moisture reserves that we normally count on to carry that crop during an extended period of dry or hot weather.

Therefore, we are looking at situations where we will probably get off to a good start. They will probably get off to an early start because there was a lot of field work done last fall. The last time we looked at this situation was 1977. And if you go back and look at 1977 as a good analog year in which we started with very limited moisture in the sub- or deep-soil moisture part of the profile, we got very timely rains and you saw the crop respond very well. That is the situation we are in today. And if you look at the long-range outlook, it looks like we will get our spring rains.

There is a major difference between this year and last year's weather patterns. And I think that is the real key to assessing what may unfold this year. Last year the storm track was far out of its normal location already in the spring months up over southern Canada. That diverted most of the storm track up over Canada. We simply missed our spring and early summer rains.

This year we find the storm track back down pretty close to where you would expect to find it during the winter months and the spring months. And we have had a series of storms that are coming across pretty much as you would expect in the spring. They just simply have not been developing in the rain as far West as we would like to see it. That is why we are seeing the dryness in the western Great Plains. But we have been continuing to add to the soil moisture in the central and eastern parts of the country.

This is an encouraging picture as we go into the spring season as we approach the planting season. And it is going to depend on the continuation of these spring rains in order to insure the 1989 crop.

Mr. GLICKMAN. So you do not project the back to back drought then?

Mr. STROMMEN. We do not have any place in the climatological records of major back to back droughts.

Mr. GLICKMAN. But we did during the 1930's; did we not?

Mr. STROMMEN. No, we saw a substantial yield recovery between the 2 worst years. In other words you see a rebound. Now it is not impossible when you are dealing with weather to get these events, but climatologically speaking going back to 1860's we have not seen back to back major agricultural droughts. The fact that we see a very different synoptic weather pattern this year than we did last year, I think, is an encouraging outlook at this point. But it is much too early to define what that final weather will be.

Mr. GLICKMAN. I know that my time has expired. I just want to make two quick points. One, Dr. Wilson you have responded on questions 4 and 5 to issues involving haying and grazing, as well as failed acreage requests and I just hope that the Department honors its commitment that you include in those statements by responding promptly, and as well as the State ASCS offices do the same thing.

My last point is I have suggested four policy options that are possible. Has the Department, as of yet, made any kind of internal determination as to proposed legislative changes which you would recommend?

Mr. WILSON. No, Mr. Chairman, we have simply not considered any changes at this point in time. I did discuss this with Secretary Yeutter earlier this week and he thinks that this is the time to monitor the situation. He is considering reestablishing the intra-agency task force that we set up in March 1988 in order to have that group ready to move if necessary. We do have a cross Government working group that has been monitoring the situation throughout the winter.

Mr. GLICKMAN. Can I get a response from the Department on these options that I submitted in the opening statement?

Mr. **Wilson**. We can submit that to your office.

Mr. **Glickman**. Thank you. Mr. Roberts.

Mr. **Roberts**. Thank you, Mr. Chairman. I should say at the outset that this may be one of the last times that we have the opportunity to work with the Assistant Secretary and you and I want to thank you for your past efforts in our behalf. There are many times that you have come to the table as you were under rather strict reins from OMB and USDA in regard to the policy and the latitude that you have and if you tried to adhere to all of the suggestions by the members of this committee, why it would be a tall order. I would simply say, good and faithful servant, a job well done.

Dr. Strommen, I really appreciate your efforts to try to help us through this with the best kind of forecasting that we can get under very difficult circumstances. We have asked the Department, both personally in my behalf with the Secretary and through staff what their stand is, what their feeling is about the legislation that I plan to introduce in about 10 minutes. And I do not think they are overly excited about it. Perhaps with some degree of common reason, we will work that out together.

I want to thank you Leo, who is from Clyde, Kansas America for taking pictures of my district. Next time let us know, we can have you do some social security work out there. And we have a picture here that we have from my colleagues, it says, visit historical Dodge City and the wheat looks lousy, and we are dry but we can always serve you a sarsaparilla, if that is the case.

As a matter of fact, I think we have a farmer here from Norton, Kansas, from a member of the Wheat Commission, Joe Berry who is sitting in the audience, and Joe why do you not talk to the doctor here, Dr. Strommen because I know that it looks good in this picture. It is green, but as my colleague from Oklahoma pointed out, that does not necessarily mean that we are going to have the kind of crop that we would want. There is an old expression in our country, by Easter you ought to be able to hide a jackrabbit in the wheat field. And that poor jackrabbit would have to run all the way to Oklahoma City to get any cover as far as the current situation is concerned.

So we do not have any brace roots. It is a lot like celery, if you took it out of the refrigerator, then you put it back in and had Meryl Streep, of course, scrub it with detergent, at any rate, what I am saying is that I just do not think we are going to have that kind of a crop and more especially, a little later we have some witnesses here. I know Dr. Schnittker is here and David Frey is here from the Kansas Wheat Commission.

And all up and down the line in terms of fertilizer, in terms of sales, in terms of chemical sales, in terms of sales of the farm equipment, we are seeing a dramatic decrease. We may well be able to quote "save" in OMB language some $400 million, but that deficiency payment is figured on the cost of production to make the farmer whole. And I come back to my basic point that if, in fact, the disaster assistance was a model for situations like this in the future, well here we are. So I would encourage the USDA to really consider this as best we can in an expedited fashion.

Obviously it is my district, my people, and I get a little wound up over this, more especially of what we saw as of last year. And so with that I have three questions for the Assistant Secretary, but I think the chairman has gone over them, i.e., can you give us the Department's early estimates on the drought's impact on the 1989 crop? And you say it is too early. Have your estimates revised the Department's projections relative to target price? And you have indicated some range there that that could go up. If the 65 percent harvest projection is accurate, a rough estimate shows about 150 million bushel reduction in Kansas, then how does that apply to the set-aside?

I can assure you that there are people out in our country who do not want to go back to fence row to fence row and would hope that you would use a very large amount of caution in that regard. Now that I have asked those three questions, you have already answered them with the chairman, I think, I will yield back and do the Lord's work on the floor of the House. I thank you.

Mr. JOHNSON [acting chairman]. The gentleman from Oklahoma.

Mr. ENGLISH. Thank you very much, Mr. Chairman. Dr. Strommen, you were talking about the fact that rain temperatures were a little cooler than normal, that we might be able to recover some of the wheat that we previously thought was damaged, and we might have a little better crop than we thought. Does that not really depend on what area you are located in the Great Plains?

Mr. STROMMEN. That is going to have a strong bearing on it at this time.

Mr. ENGLISH. If you are located in the southern part of the Great Plains, the southern part of the Hard Red Winter wheat producer area, then you are much further along the process. In Oklahoma, why looking at it we are probably a month and a half away from beginning harvest. So the chances of our recovery are much worst than they would be say further north in the wheat harvesting pattern; is that correct?

Mr. STROMMEN. That is correct.

Mr. ENGLISH. So it is conceivable at this particular point, I should not say conceivable, it is a fact that this particular point that it is much easier to predict the kind of crop that we are going to have in Oklahoma than it would be say much further up the Great Plains?

Mr. STROMMEN. That would be correct. And I must add that the late freeze that you had in parts of the extreme western Great Plains of the Oklahoma Panhandle down into the Texas Panhandle did some additional damage recently to the crop and that is an unknown at this point. We really cannot tell you what that damage was until we get into the harvest.

Mr. ENGLISH. The reason that that caused a problem was due to the fact that we did not have the subsoil moisture and therefore there was little or no root system. Everything was pretty much laying on the ground.

Mr. STROMMEN. In part it was and in part it was because the crop was sufficiently far along that you do not have that potential to recover.

Mr. ENGLISH. Mr. Wilson, in looking at the question as we have provided in the 1988 drought bill, in order for a farmer to be eligible he has to have 35-percent loss, as far as that crop is concerned. That is a pretty heavy loss; would you not agree?

Mr. **Wilson**. That is a significant loss.

Mr. **English**. Therefore, would it not make sense from the consideration of drought legislation that it really does not make any difference at this particular point as to this particular situation from the standpoint of loss. What I am getting at is 35-percent loss is 35-percent loss. It does not matter whether you are talking about one county or you are talking about half a State or whether you are talking about a region in the country. It is a loss. And the farmer that suffers that loss has a disaster; is that correct?

Mr. **Wilson**. No question that for the individual farmer who suffers that loss, it is a disaster.

Mr. **English**. So in considering legislation and talking about perhaps extending the 1988 bill to apply to crop year 1989, for those who say well let us wait and see how severe the drought is, the legislation itself takes care of that. If the person does not have 35-percent loss, he is not going to be eligible. Therefore, it will apply to only those people who truly have a disaster; is that correct?

Mr. **Wilson**. Now this is related to the 1988 crop. We do not have any disaster provisions for 1989.

Mr. **English**. I realize that. I am talking about if as far as extending it; is that correct?

Mr. **Wilson**. Yes. If you extended the 1988 Disaster Act to 1989, then with the same terms, then it would have to be a 35-percent loss.

Mr. **English**. So no matter what happens to the development of the rest of the crop, whether we have recovery in the far northern regions of the wheat producing area and they may turn out to have a great crop, the fact of the matter is those farmers who have a 35-percent loss or more are suffering a disaster. And what we need to do if we are going to be fair and provide the same kind of fairness to wheat farmers this year that were provided to farmers last year, is basically extend the program; would that be simple justice?

Mr. **Wilson**. It is too early though to be sure that we are going to have the kind of broad-based losses that you are talking about.

Mr. **English**. But the point I am making is that it does not make any difference. The 35 percent itself, if a person does not have a 35-percent loss, he is not going to get any benefits. Therefore, even if we have this recovery for the farmers that is wonderful. If the entire region somehow miraculously—the soil rises and we have wheat produced and nobody has a 35-percent loss, then the program itself takes care of that. There is nothing that is provided for the farmer; is there?

Mr. **Wilson**. It would be nice to always protect farmers from loss and to make this a risk-free world, but as a Nation we simply cannot afford to do that. One of the purposes of insurance is to try and protect against those individual losses.

Mr. **English**. You have already told me though, Mr. Wilson, for that farmer it really does not matter whether it is his farm alone or the western half of his State or the whole region, he is going to suffer the loss. The impact on him is going to be just as great. So what is the difference between applying it to that one farmer as opposed to applying it to an entire region. Why from a simple justice and fairness standpoint, would you simply say, hey Mr. Farmer, we are not going to give you any help unless the whole region needs help.

Mr. WILSON. As a Nation we simply cannot afford to indemnify everyone against any loss at any time, even if that loss is terrible for that individual.

Mr. ENGLISH. Then how can you justify doing it for a region if you are not willing to do it for a single farmer?

Mr. WILSON. I guess I do not understand the question. We have no disaster provisions that are in effect today. The 1988 provisions have expired.

Mr. ENGLISH. But we have already agreed here that we have a very serious situation. We already agree that we are likely to see numerous farmers, not a single farmer, but whole parts of States in which farmers are going to be suffering 35 percent losses or greater. Now we know that much.

The point that I am making is the bill itself grants the benefit only to farmers who have a 35 percent or greater loss. That being the case, how can we out of simple justice sit here and wait for some kind of estimate further down the road to see how great the disaster is? Does not simple justice demand we know there is going to be a disaster, we know the people are going to be effected, the only question is how many? And therefore, why do we not simply go ahead and extend the 1988 program and cover those people that we know are going to have this disaster?

Mr. WILSON. We do not know that there is going to be a widespread disaster. That is highly uncertain at this point in time. We can predict that there will be individuals who have a disastrous year, but I could say that at this time any year.

Mr. ENGLISH. OK, let us go back then and tell me then how many folks does it take for the Department of Agriculture to agree that assistance ought to be provided to a single farmer? How many of his neighbors have to be included before he can expect the Department of Agriculture is going to smile on him and say, yes we will help you, you finally got enough farmers in enough trouble, we are going to help you. What is that number?

Mr. WILSON. It would be very nice to be able to protect all farmers. We simply cannot afford to do that.

Mr. ENGLISH. I am not asking you that. What is the number?

Mr. WILSON. There is no such number.

Mr. ENGLISH. Let me ask you this. Is the Oklahoma Panhandle sufficient for the Department of Agriculture to support a disaster to extending the 1988 disaster bill? Is the Oklahoma Panhandle by itself enough?

Mr. WILSON. Well, it seems to me that is a legislative question, Mr. Chairman. It is not a question for me. That is a question for the legislature to address.

Mr. ENGLISH. The Department of Agriculture has a big impact over here whenever they come over and say, yea or nay with regard to legislation. Will the Department of Agriculture support extending the 1988 bill to 1989 if only the Oklahoma Panhandle, the three counties in the Oklahoma Panhandle are effected; will they agree to support it? Is that sufficient? Is that enough counties for the Department of Agriculture to agree to support this legislation?

Mr. **Wilson**. As I indicated to the chairman earlier, this is a situation that we are monitoring. When I discussed it with the Secretary——

Mr. **English**. I am asking you a simple question. How many counties does it take for the Department of Agriculture to say, yes, this is a sufficient enough disaster, we are going to support disaster legislation? Or no, that is not enough people that are going to be affected, therefore, we are not going to support it. How big a disaster does it have to be is what I am getting at? I have farmers in my area who are already to the point where we know we are going to have a disaster. We are far enough along in production, there is no question, we are going to have it. We have wheat blowing out of the ground. It is ending up blowing 60 miles down the road, so it is not even going to be there. How many counties does it take, Mr. Wilson?

Mr. **Wilson**. Under normal circumstances, and this is part of long-term legislation, it is not the 1988 Disaster Act, a county has to have a 35-percent loss. Those are the normal rules.

Mr. **English**. That is what I have been saying. The question is, though you have told me where a single farmer out there on the farm who has a 35-percent loss or more, that is not enough farmers to get the approval of the Department of Agriculture or the blessing of the Department of Agriculture for extending the 1988 disaster bill to cover it?

Mr. **Wilson**. Not under the current statute, no.

Mr. **English**. I did not say under the current statute. I said the support of the Department of Agriculture. The blessings of the Secretary of Agriculture. The encouragement of the Secretary of Agriculture. Now you have said, if this thing is big enough, you all will support it.

The question I am trying to determine is we know that you will not do it for one farmer. We assume you are going to do it for a dozen States. Now the question I am trying to narrow down is, at what point do we finally reach the level that the Secretary says that is enough? That is enough farmers, we will support it. That is enough farmers getting a 35-percent loss each or greater to finally support legislation or extending the 1989 drought.

Mr. **Wilson**. That is a very academic question, and I just do not have an academic answer for you, Mr. English.

Mr. **English**. So our farmers will just have to guess as to whether or not this drought extends to enough counties and enough States to get the blessings and support of the Secretary of Agriculture and the administration to extend the 1988 drought bill to provide the same protection that we provided for farmers last year; is that true?

Mr. **Wilson**. We will have to monitor the situation and see if it rains this spring and see how bad it is before we do anything.

Mr. **English**. How bad it is. How bad it is for whom?

Mr. **Wilson**. For the farmers. I have great sympathy for these farmers.

Mr. **English**. I know that. You have told me that. How many farmers? How many States? How many counties?

Mr. WILSON. Look, I do not have any numbers. It is a judgment that would simply have to be made as we go along, but this is something that we need to monitor and watch from day to day and that is what we are doing.

Mr. ENGLISH. So we are waiting on the Secretary of Agriculture to get up some morning and feel inspired and say, oh my goodness, I think we finally got enough farmers in trouble that we will extend this protection; is that right? Thank you, Mr. Chairman.

Mr. JOHNSON. The gentleman from Missouri, Mr. Volkmer.

Mr. VOLKMER. Mr. Wilson. I am not going to really continue with the questioning from the gentleman from Oklahoma.

Mr. WILSON. I am pleased to hear that, Mr. Volkmer.

Mr. VOLKMER. Even though sitting here, it is a little amusing to hear, and I thought maybe you were going to say, we have to run it by OMB first.

Mr. WILSON. Not me, sir.

Mr. VOLKMER. Or the Secretary, somebody else that has something, because we did have the administration's support last year. Of course, it was election year and I do not know if that had anything to do with it or not. But we did have the administration's support for that disaster relief bill.

Mr. WILSON. It was the worst drought since the 1930's, Mr. Volkmer. It was a terrible tragedy.

Mr. VOLKMER. I know, but if a tragedy and I think like the gentleman from Oklahoma was trying to get to, to the individual farmer, it is his tragedy, no matter how many of his neighbors or other farmers are effected. I think that is what the gentleman from Oklahoma is trying to say.

Mr. WILSON. I think, let us be realistic, it has to be very widespread before it grabs the national attention. Much as that is unpleasant to the individuals who are afflicted by that tragedy, but I can find any number of individuals in the United States today who are afflicted by tragedy.

Mr. VOLKMER. Let us get on to something else. Right now the target price for this year is $4; correct?

Mr. WILSON. Yes, sir.

Mr. VOLKMER. What is the current loan rate, $1.90?

Mr. WILSON. $4.10 this year. Projecting $4 for next year.

Mr. VOLKMER. It is $4.10. What is the current loan rate dollar?

Mr. WILSON. $2.06.

Mr. VOLKMER. What is the market price?

Mr. WILSON. In March we were looking at prices that were somewhere about $4.10—between $4.10 and $4.20.

Mr. VOLKMER. Yes, but I mean even in July; are we not looking at better than $3 prices?

Mr. WILSON. Certainly.

Mr. VOLKMER. Do you envision that the market price next year will be any where near $2.06 because of what is happening?

Mr. WILSON. No. I would predict at this time, it would be higher than that.

Mr. VOLKMER. In excess probably of $3, when we get down to that?

Mr. WILSON. That would be my present prediction, yes.

Mr. VOLKMER. Based on what is going on. Based on last year's drought, the shortage, the fact the feed shortage, et cetera, the fact that it looks like we are going to have some wheat shortage, if we do have that, that loan rate is really not going to mean very much is it? Except as a tool for farmers to use in order to hold their wheat off to market and wait for maybe a higher price later on, but other than that, it is not going to mean very much; is it?

Mr. WILSON. The loan rate at that point becomes what is intended in the law, a safety net below the market price. That is the principle.

Mr. VOLKMER. You do not envision too many farmers letting the Government take their wheat for $2.06?

Mr. WILSON. No, I think most farmers would be more happy selling their wheat for a higher price.

Mr. VOLKMER. That is right. That is what I am getting at. And the export market is not going to condition on that loan rate? So the market price is going to be so much higher.

Mr. WILSON. Certainly. The loan rate will not be an impediment to us exporting next year.

Mr. VOLKMER. That is correct. That is my point. If I put that loan rate up to $2.50 or to $2.70, it is not going to mean a thing.

Mr. WILSON. It depends on what happens 2 or 3 years down the road. It may not mean a thing in 1990, but I suspect by 1995, you would be back into the problem you were in 1981.

Mr. VOLKMER. I am just talking about 1990, and the reason I am saying that is we have got some budget problems and I might be able to get some credit and do some things besides doing what the administration is proposed to do, reduce target prices. I might be able to raise the loan rate a little bit, have no effect on the total economic conditions of agriculture on it at all and still save money.

Mr. WILSON. As a philosophical matter, we have deliberately allowed loan rates to come down and in fact we now figure them as a moving average of previous market prices in order for the United States to be competitive in the long run. That is the current philosophy of our pricing policy and it would be a mistake to reverse that and start increasing loan rates.

Mr. VOLKMER. With the market price as high as it is going to be?

Mr. WILSON. As high as it is going to be this year, but we simply do not know what it is going to be 2, 3, or 4 years from now.

Mr. VOLKMER. You are hoping for lower market prices; is that what you are telling me?

Mr. WILSON. No. I am not saying that, Mr. Volkmer. But I think you have to be realistic. If we price ourselves out of the world market that is not good for American agriculture.

Mr. VOLKMER. I disagree with the fact that we will be pricing ourselves out. We do have the EEP. Thank you. Thank you, Mr. Chairman.

Mr. GLICKMAN. Mr. Wilson, I think we are finished now with this panel. I would say this—that you ought to take back to the Secretary—I think he will probably be coming back this weekend?

Mr. WILSON. Yes, he will.

Mr. GLICKMAN. The following messages—one is that we will naturally want to talk to Congressman de la Garza, the chairman of the committee to determine how he wants to proceed, but we do not want to fight the Department on these things. I think we do have a genuine disaster in certain parts of this country, and I guess my point in my opening statement was is that we want to be able to try to develop a package and maybe hold for a while to see how the weather turns out to determine how we structure this thing, and not to engage in some form of Pennsylvania Avenue warfare from the Department.

I am not saying you have been in any way more than helpful to us. You have been extraordinarily helpful to us. But there are a lot of us who feel that the same conditions that we had last year are with us this year. It just may not cover as many States, but the hurt is every bit as big as to those people who are affected. So we hope the message gets back there in a way you all were of most cooperative in the 1988 disaster bill. We expect that kind of cooperation this year, as well.

Mr. WILSON. I will tell Secretary Yeutter that you are very concerned about the situation and that you would like to proceed with legislation. I am sure he wants to work with you, but I do know he does not want to do anything precipitous. He wants to watch this situation unfold before we get too far into legislative change.

Mr. GLICKMAN. Mr. English.

Mr. ENGLISH. Thank you, Mr. Chairman. Mr. Wilson, the point I was trying to make to the board is that I am getting the feeling or have had the feeling that basically in order to receive assistance from the Federal Government, from the administration, and Department of Agriculture that we have to have a disaster that reaches a certain decimal level with the media. If this disaster has not been on the cover of Time and Newsweek, it does not qualify as disaster and therefore there is no assistance forthcoming. And I think that is wrong. I think it is a wrong way for us to approach these problems.

We have talked about the Crop Insurance Program. Crop insurance is available. The fact of the matter is in many parts of this country crop insurance simply does not work. It does not make financial sense to the farmers to buy it. Now that is not the farmers fault. It is because of the program and we know that. We have a commission established to deal with it, and we are going to try to deal with it.

And it is as I said when I opened up. We feel like we can put together a program that in fact will serve the farmer. But the fact of the matter is it is not going to be available to those people that are suffering under this disaster and the communities and the States that are involved because it effects the entire economies of these States. Most of these are major agricultural States.

And therefore, under these circumstances, and I think we have got to take a little different approach, I think the fairness itself dictates that we extend the same helping hand to the farmers that are affected this year that was done last year. Many of us strongly supported it even though we were not affected, even though we did have good crops. We understood disasters and certainly from our part of the country, we understand.

So the bottom line was that I would hope that we would not get into this question of how many farmers or how many counties or how many States are impacted or whether it has been on the cover of Newsweek or Time or how many national TV shows it has been on too. I just think it is a wrong way to approach this, and knowing the Secretary, quite frankly, I do not think the Secretary is that kind of man that would do that.

But the point that I was making, I think, there are a lot of folks that are beginning to draw that kind of conclusion and I think that the Secretary and the Department ought to step forth very quickly to assure people that in fact it recognizes a disaster for a single farmer is just as severe as it is for five States of farmers. Thank you, Mr. Chairman.

Mr. **Glickman**. One other thing too. The potential savings because of this drought is quite high if the worst scenario happens. And then of course we do not want the worse scenario. You pointed that out in your statement. Again, I repeat your numbers were meant to be hypothetical and not to represent the Department's point of view.

But right now, as we talk about these potential savings, while we are already talking, the Budget Committee of the House is meeting with Mr. Darman and OMB to look at how we can come up with savings in the ag budget. The reason why it is important to get you all on record as quickly as possible as to what policy options you would put down is because we could get ourselves trapped in for the 1990 budget of taking advantage of the budget savings for the drought for the purposes of complying with the Gramm-Rudman law. I want to make sure that does not happen here.

If we have to make cuts in agriculture, they ought to be made across the board in connection with general policy and not prejudice those who have suffered a drought. So that is why I think it is important that we know fairly soon which way the Secretary would be inclined to go and then we can wait to see what the weather damage ultimately is. I think that is fair, and as I said before, we have to live within responsible budget constraints as well.

So we appreciate your coming down here and also appreciate your complying with the committee's request on those specific interrogatories that we asked you. We will be in further touch. Thank you both. Thank you, Dr. Strommen, and thank you for coming down again.

Next we have a panel of Dr. John Schnittker, Schnittker and Associates, as well as David Frey, assistant administrator of the Kansas Wheat Commission in Manhattan, Kansas. It is a pleasure to welcome everybody here. First of all, John it is a pleasure to welcome you here. John Schnittker, of course, has a career in agriculture far greater than I do. And we are delighted that you are here.

David, we are delighted that you are here from Kansas and I believe that you were on a tour of the States' wheat crop, along with some other folks. So we would like the benefit of your point of view too. We have another gentleman.

Mr. **Frey**. We have the Chairman of the Kansas Wheat Commission, Mr. Joe Berry.

Mr. **Glickman**. Yes, we are delighted to have you here as well. I think what we will do is we will start with John Schnittker, and then as you are listed. So John, you can begin.

STATEMENT OF JOHN A. SCHNITTKER, SCHNITTKER & ASSOCIATES

Mr. SCHNITTKER. Thank you, Mr. Chairman. I have a four-page statement which I assume can be included in the record.

Mr. GLICKMAN. It can.

Mr. SCHNITTKER. And a brief summary. I believe that the Kansas crop has declined now from a potential of about 430 million bushels to about 275 million bushels and still falling. The U.S. Winter wheat crop, I think, has been reduced from a potential of about 1,850,000,000 to perhaps 1,600,000,000, a little lower than the Department of Agriculture said a moment ago.

I think with good weather from now on, including the Spring Wheat Belt, the total wheat harvest will be at around 2.25 million bushels, just below USDA's 2.3 million bushels. I think U.S. carryover stocks could easily be reduced to 400 million bushels and with a little trouble in Spring wheat or the rest of the world to pure pipeline stocks of say 200 million bushels, without much damage to wheat elsewhere.

As a result, it seems clear to me already on April 6, that we are forced to increase U.S. wheat area for 1990 to or near the maximum level under the program, that we ought to suspend or to slow the contracting of further wheat land in the Conservation Reserve since we already have 10 million acres contracted and little excess capacity left in the wheat area. And we ought to conduct any EEP operations in the next few months with great discretion.

We may be able to export our wheat supply without substantial subsidies during the next year and in any case, we can always restart the EEP in June or July if U.S. and world crop conditions improve.

We should examine the issue of grain reserves in the year ahead, both for the United States and the world. With stocks depleted the decks cleared of surpluses, and the farm bill debate pending, I think we have an unusual opportunity in this area of grain reserves.

Regarding the drought steps. It seems to me it is routine to extend the sign up for a few days if that becomes necessary. That would tend to be more applicable for Nebraska and South Dakota than perhaps Oklahoma or Kansas, but still it could be done. Clearly, the savings on deficiency payments will go a long way toward extra payments on drought relief, and I urge the committee not to overlook the savings from higher feed grain prices resulting from reduced wheat supplies which could also be attributed to general savings from the drought.

Finally, I am going to say that it seemed that the Department of Agriculture witnesses implied that the Winter wheat crop in the damaged area could still recover substantially from the 280 million bushels that they mentioned for Kansas. It is my belief that the Department's estimates, as well as mine for any moment in time, imply good weather from here on out, and that we are going to get the 4 inches of rain per month, and reasonably good temperatures. And therefore, I would question that from whatever the number is on April 6, for Kansas or for the whole Winter Wheat Belt, that only a little recovery is possible in the drought area. Thank you, Mr. Chairman.

[The prepared statement of Mr. Schnittker appears at the conclusion of the hearing.]

Mr. **Glickman**. Thank you. Please proceed, Mr. Frey.

STATEMENT OF DAVID FREY, ASSISTANT ADMINISTRATOR, KANSAS WHEAT COMMISSION, ACCOMPANIED BY JOE BERRY, CHAIRMAN

Mr. **Frey**. Thank you very much, Mr. Chairman. There was already mention made of Kansas' wheat production. Some years we grow more than Australia and some years more than all of South America. This past year in Kansas we planted 12.4 million acres of wheat in the State. That is not any where near what we have planted within our record years, but that is an area of 193 miles by 100 miles of wheat plants. And if it grew to its historical potential, I think, we heard already what that probably would be about maybe 11.4 million acres harvested, about 38 bushels to the acre for 433 million bushels. At $4 a bushel that would have been a $1.7 billion influx onto the farm in Kansas.

Of course, it will not be like that this year. But we could have used that kind of influx into our rural economy in Kansas. Times have been hard on the farm. I know you in Congress have very big issues to chew on. You have to balance expenditures and set priorities, "guns or butter," put things into perspective. And I want to share with you some of the perspectives on U.S. agriculture.

In the 1980's, insurance companies told us that farming overtook mining as the most dangerous occupation. Economic conditions have been such in America that we have lost more than 1 million farmers in the 1980's. We now have fewer people living on farms in this country than any time since the Civil War. In Kansas we have had agricultural crises centers set up in our State. Now that is not new, but we never used to have anything like that before. And just over half of Kansans living on farms also hold jobs off the farm. This year even with relatively better commodity prices this trend will not change. This drought that we are experiencing in subsoil moisture, this very severe drought that we are having was proceeded by a much longer drought of low farm prices.

Before we get to some of the details about how our current Kansas crop conditions will affect our economy, allow me one more very important perspective. And that is that food prices in the United States, of which approximately 25 percent goes to the farm, 75 percent to the food processing and the food service industry. Food prices figured as a percentage of disposable income are lower in the United States than in any other country in the world and they are the lowest in the history of this country.

Americans in 1987, latest figures, had $3.2 trillion after taxes to spend and 12.1 percent of that had to go to food and that includes eating out. And 1987 was a year when we heard much about $27 billion going for agricultural subsidies to the farm. It has gone down since that last year. But if you throw that $27 billion of agricultural subsidies in with what was spent on food, we still spent less than 13 percent of disposable income on food in this country.

So I have some questions. Is the United States subsidizing agriculture? Or, is the loss of the 1 million American farmers in this decade clear evidence—that even from the mix of market and Government prices—American agriculture has not been sufficiently recompensated for service to this country? And have farmers not been recompensated to a level that allows agriculture to remain viable?

Now we went into this year, 1989, from of course a very dry 1988. We were fortunate to have a normal 1988 wheat crop in Kansas considering the large acreage reduction. But we had a record warmth in January, record warm temperatures. A lot of the wheat came out of its dormancy. This kind of set up a lot of the wheat, especially in north central Kansas for some record low temperatures in February. In fact, in Russell, Kansas, for example, the temperature dropped 100 degrees in 36 hours by the first part of February. This is why we are talking about winterkill. And when we went out to the fields a couple of weeks ago on that wheat tour, I was fortunate to be with plant pathologist from Kansas State University, Dr. Gary Paulsen. He cut into the crown root and looked at the wheat plant and the color of the growing point. And although we were getting some greening up in some of the fields, there was some discoloration in many of those plants and this indicated that this was not going to make wheat.

I want to look at what we have got so far and I know we had the good report on the weather, but Dr. Rollie Sears who is our wheat breeder at Kansas State University notes that normally when we plant the wheat crop, there is subsoil moisture down 3 or 4 feet under ground. When we go 3 or 4 weeks without moisture, subsoil moisture acts as a canteen for the wheat, but because of the lack of rain this year and the lack of subsoil moisture, we are going to have to live from rain to rain. It is going to have to rain frequently, to get us through the growing season.

To start with the good news in Kansas, and that would have to be eastern Kansas, we have reports from several of our wheat commissioners and in eastern Kansas from John Junior Armstrong, he said, as you know, probably we are the exception as to the wheat conditions in Kansas. Our wheat looks good, it is a little late, has excellent color and is growing. We had over 3 inches of rain and it came easy and it all soaked in. And he said a conservative guess is 90 percent of normal in eastern Kansas. None of it that he knows of is being abandoned. The pastures also look good, he says. We have to remember that eastern Kansas, the eastern third of Kansas, averages about 10 percent of the wheat crop in the State.

Now, let us look at where the wheat-growing areas are. And right out in the middle of the wheat-growing area we got a letter from St. John National Bank, Stafford, Kansas. He said we expect only 15 percent maximum of the normal wheat crop in Stafford County. He said, we have a $12 million loan portfolio, missing the wheat crop will directly result in an estimated $1.2 million loan portfolio loss of that reduction. However, the greater impact will be the inability of the farmer to service payment debt to real estate and machinery. And this will adversely affect an estimated additional $4 million in loan our bank has as an example. At these levels the bank then can become an economic victim along with the small town Main Street, the ugly domino effect. And he notes that all efforts to lessen the loss of wheat crop are greatly appreciated and we need the help.

There was a survey performed by Farmway Co-op in Beloit, Kansas, of their directors and their managers and they took this independent survey of their directors and their managers at the meeting and they took the average percent that these guys estimated the wheat was going to be destroyed, and they estimated that 36.2 percent of the wheat crop in their area was going to be destroyed and harvested about 63.8 percent, and of the remaining 63.8 percent of what was planted, the average yield was estimated to be 18.2 bushels per acre, if we get ideal rainfall between now and wheat harvest.

We received a letter from the Exchange Bank of Lenora, Kansas, and he underlines a very big concern in this area that pastures survive the spring that it will appear that our moisture profile will not sustain many days of grazing, and it is our observation we have 30 days or so of grazing of dry grass. And we are fast approaching the time of year when rainfall moisture efficiency is going to decrease rapidly. We are concerned about summer grazing and backgrounding programs. And so far we discussed just the farm aspect of this pie. He notes later on in the letter that the retail businesses up and down our Main Street and surrounding area are going to really feel the effects.

From our commissioner in Colby, Kansas, Harlan Sloan estimates 25 percent of the wheat has either been stripped, worked solid or already plowed up on March 30. Quite a few fields have blown enough to nearly fill the road ditches on the east and south boundaries of wheat fields, and some blowing fields have not been worked but chisels are sitting in the fields.

From southwest Kansas, our Commissioner Kent Eddy, notes that irrigated wheat in southwest and west central Kansas is in poor shape. On furrow irrigated wheat, the wheat on the top of the ridge is gone. In the furrow the wheat is in good shape; 60 percent of the furrow irrigated wheat is in this condition. He says that the wheat on the ridge represents 50 to 70 percent of the area in a furrow irrigated field. And he says the center pivot irrigated wheat is not that way; 50 percent of the center pivot irrigated wheat looks fair to good; 50 percent is poor.

In most cases the dryland wheat is in very poor condition in southwest Kansas; 52 percent of acreage is dryland; 48 percent irrigated. And he notes that one-half inch of rain, and we had probably about that much recently, one-half inch of rain will start many weeds with the thin stands of wheat. And the weed competition is going to be intense. The crop is behind schedule with regard to development stage, in some cases, as much as 4 months. I will underline that, with some comments from the wheat tour, we heard from people that noted that.

Every place in the world that can grow Winter wheat does, and the reason is because of the long-growing season. What we have here because of this late freeze that we had in February and the extremely dry conditions in the fall where the plant did not really develop, we have an extremely late crop all over the area and is similar to basically trying to grow spring wheat in Kansas. And that does not work very well as far as the yield potential, especially if we get some hot weather early, we could have significant reduction of the potential of the crop.

I am going to read from our Commissioner's report from Solomon, Kansas, Commissioner Harvey Wood. He said the drought of 1988 and 1989 had a drastic effect on the local communities. The rural communities are just beginning to recover and stabilize from the great farmer fallout when the drought hit. The drought has had both a ripple and a domino effect on rural Main Street in the Central Plains. Farm families, as well as every business, suffers to some degree. Even those farmers with high level crop insurance can only be guaranteed slightly over half of their normal crop income.

And he gives the example of 36 bushel wheat yield at $4 a bushel versus 75 percent protection at 27 bushel guarantee at $3 per bushel. When the money is not available a survival strategy is implemented. Banks, elevators, implement dealers, supply stores, including even our churches and hospitals suffer hardships and many will not survive. He sent us a piece of paper that was part of my submitted testimony. That the following is from a group of elevators in seven North Central Kansas counties reflects how the drought has drastically changed their output of sales of fertilizer, chemicals, and applications.

These figures reflect the severity drought has had upon the agribusiness community. I will just cite a couple of the numbers. Fertilizer tonnage is running at about 7.8 percent of 1988, for 1989 in this area. Sales of fertilizers is running about 7.4 percent of what it was in 1988. In other words in 1988 they sold in the first 3 months of the year $479,814 worth of fertilizer. In 1989, they sold $35,289 worth of fertilizer. The sales of chemicals, 3.9 percent of 1988. Sales of custom applications, 4.1 percent of 1988. You see certainly in that area, we have got a disaster.

I will close with a statement of an economic principle, there is no such thing as a free lunch. Are we fooling ourselves as a Nation? We were investing 12.1 percent of our disposable income on food and calling that good. Meanwhile cutting back on Federal funding of basic agricultural research and extension outreach programs. Do we not have to also stand up to Europe on agricultural trade policy to assure markets for this huge production machine that we have in the United States? And it is hard enough to make those 193 by 100 miles of wheat in Kansas pay for itself when there is a crop. When there is not one, it is just common sense that the people that take care of that land, America's bread basket, need support. Thank you, Mr. Chairman.

[The attachment follows:]

	FERTILIZER TONNAGE		$ SALES FERT.		$ SALES CHEM.		$ SALES CUSTOM APP.	
	1988	1989	1988	1989	1988	1989	1988	1989
January	276	91	$ 29,377	$ 9,908	$ 21,750	$2,431	$ 3,706	$1,679
February	607	116	80,178	12,095	37,248	4,037	20,770	1,599
March	3,359	125*	370,259	13,286*	232,541	5,000*	103,085	2,000*
TOTAL	4,242	332	$479,814	$35,289	$291,539	$11,468	$127,561	$5,278
1989 as % of 1988	7.8%		7.4%		3.9%		4.1%	

* Estimated

Mr. GLICKMAN. Thank you. Mr. Berry, do you have a statement?

Mr. BERRY. No, he made our statement for us.

Mr. GLICKMAN. Thank you. A couple of quick questions. Do you take issue with the Department's weather guidance, any of you, in that with relatively normal rains and that would be under his terms mean 30 days not as good as it should be, but the next 60 days, that we will have a dramatic improvement in the crop. I mean, I got that impression from the Department that, I think, we need to wait some time before we pass the bill because we want to see exactly what happens, but judging from your view of the Kansas wheat crop in the tours that have been taken, do you think that the crop is poised for recovery with rain?

Mr. BERRY. A certain amount of it is beyond recovery. In my novice observation, I have only farmed for about 40 years——

Mr. GLICKMAN. Then you are not an expert?

Mr. BERRY. No. In my area, I would say that we are 20 percent damaged.

Mr. GLICKMAN. You are from where?

Mr. BERRY. Norton County.

Mr. GLICKMAN. So you are 20 percent irreparable damage?

Mr. BERRY. Right. I am losing about 1 or 2 percent a day.

Mr. GLICKMAN. The interesting thing that I think we all have to remember is that even the 1988 disaster bill that we passed requires a 35-percent loss before you trigger in any assistance whatsoever. I want people to know that no matter what kind of program we pass, there will probably be a threshold on loss before you could come in. There are vast areas of the State in the country that would not even qualify under that 1988 Disaster Assistance Act. It is important to remember if we use that as a formula, and it may be the one we have to use because of fiscal constraints. It does not certainly allow anybody to be made whole.

But anyway your testimony is that there is some that is irreparably lost. Your area it may be about 20 percent. Mr. Frey do you have any additional comments on that?

Mr. FREY. I would say that north central Kansas, I think you have some real extreme examples like this area around the Farmway Co-op, where you have close to 40 percent already, is basically not even going to be harvested and the rest of that, and I would say that the substantial part of that is freeze damage. I also feel like there are a lot of people that are looking at this green field phenomena and not realizing that the growing point of the wheat has been killed, and it is not going to make a wheat crop, and that freeze damage has already happened.

Mr. GLICKMAN. Let me ask you. Will wheat that is late developing grow to normal height or will it be stunted?

Mr. BERRY. It will be stunted.

Mr. GLICKMAN. What is the effect on yield on stunted wheat?

Mr. BERRY. By stunted I mean it will not get quite as flat, but it will also reduce the yield and you have no way of guessing or gaging how much it will reduce the yield, but you also have to consider that you cannot harvest short wheat as well as you can tall wheats.

Mr. GLICKMAN. So even wheat that is greened up now may end up being short wheat?

Mr. **Berry**. Right.

Mr. **Glickman**. And there is no way to determine the quantity of that just yet; is there?

Mr. **Berry**. I am also a custom harvester, so I know a lot about short wheat. When they do have droughts in certain areas, you can lose up to 10 percent of the yield of the wheat because it is so short you cannot get it in your machine to harvest it.

Mr. **Glickman**. Let me at this moment ask—Mr. Schnittker. You talked about increased acreage, the way we may have to do it to deal with some of our international problems and everything else, but does not increased acreage drop prices, increase cost of the program?

Mr. **Schnittker**. If we have quite a high price this year, then it seems to me that we would have to look for a lower price for the 1990 crop if we had more acreage and a good crop. That would also increase the cost of the program, as you said, and that would be a tough hurdle to get over because the OMB and everyone else will find it difficult to cough up more money for the wheat program. I think that adding to wheat stocks or corn stocks, when they have been reduced to extremely low levels ought to be looked upon as an investment in stabilization, in food security, not as an expenditure for farm programs. I know that is a difficult hurdle to get over.

Mr. **Glickman**. You talk about that in terms of we ought to consider this as more of the capital expense rather than an operational expense?

Mr. **Schnittker**. Exactly.

Mr. **Glickman**. Unfortunately the United States does not allow us to do that.

Mr. **Schnittker**. But once you have accumulated 100 million bushels of wheat and we seemed to have spent $300 million for it, we are going to get that back in a few years when these 100 million bushels come to our rescue following a drought.

Mr. **Glickman**. On the question of EEP, you indicated to John that it may be time to use it more judiciously. I think this is paraphrasing what you are saying. I am just curious, now we are in a time when we are engaged in these bitter battles in Europe and trade matters, is now the time to drop it off and if we were to drop it off from a commodity point of view, should we establish some sort of a cash program, just from a trade point of view?

Mr. **Schnittker**. I think the wheat situation we are getting into in the United States and the world is one in which we can no longer keep world wheat prices low in any general sense of the word. Therefore, we cannot use the EEP in the wheat circumstances that may develop to force the Community to improve its agricultural policies. So I think we have to declare a little holiday on that objective of our EEP program in the event wheat is very scarce. We ought not sell it to the world for less than we can get for it.

Mr. **Glickman**. Dave, I want to go back to you or Mr. Berry. Does increased acreage guarantee higher production of wheat just by going down to a lower ARP? Does it guarantee higher production of wheat? And what does the increased acreage do to conservation practices and weed control efforts to farmers?

Mr. **Berry**. Well, increased acreage does not necessarily guarantee increased production. As you will note, this year in Kansas we planted about 12.4 million acres of wheat and I forecast that we are going to be—somebody said 275 million bushels. I think that is optimistic. And yes, reduced set-aside does have quite an effect on your weed control.

Mr. **Glickman**. Weed control; right?

Mr. **Berry**. Right.

Mr. **Glickman**. You see that is the point I think we have to be somewhat careful about, about the expanded ARP's. I think we have to look carefully to what we really get out of going from 10 to 5 or 10 to zero.

Mr. **Berry**. I certainly agree with that.

Mr. **Glickman**. Let me go finally to this question of options, what we ought to do. I think that all of you ought to comment on this. I have said that there are at least four options. There may be more options that Congress could do in addition to what the administration can do themselves.

One option is to just extend the 1988 Disaster Program to 1989. We could do that for all crops or we could do that for Winter wheat only. And I am not saying what is feasible. In doing that, that brings us into a program that provides a 35-percent threshold before any payments are made, and then you have essentially the payment of 65 percent of your loss after you have reached that 35-percent threshold. So it is a rather incomplete recovery, but it is better than nothing. That is one option. That is what we did with corn. That is one way we would go down the wheat program.

Another option would be essentially taking the 0/92 program and making it the guaranteed payment higher because under 0/92 we may not have much of a payment this year. So we could go that route.

A third option, which is difficult because of the way crop insurance works, but it is one that may have the best public policy implications, is to reopen the Crop Insurance Program for the 1989 wheat crop and let people in who did not come in. And of course, the payments under that with yields and premiums and everything else may not be much better than the Disaster Program, but it does tend to get people into thinking that this is what we are going to do. From now on folks, we are going to provide crop insurance and you better get into it because you cannot count on Uncle Sam coming up with a Disaster Program every time that there is a problem. And therefore, we are going to give you a little stimulus. We are going to say, reopen it so you basically get to buy it retroactively in a sense after the house has burned down, but you still have to make the premium payment and do all those other things. And there is a little risk because we do not know how much damage will be there. We could open it for 4 weeks or 6 weeks or whatever.

The Department may have the authority to do this themselves, the Federal Crop Insurance Corporation may have the authority and we have not got the determination on that.

I wonder if any of you have any comments on any of these proposals or anything else that we might do. I might mention again, my goal in all of this is while Congressman Roberts has dropped the bill in, my goal is to talk to the chairman of the committee, Congressman de la Garza and try to figure out if we can come up with a consensus thing that could move when and if we see that the problem is ready to go. So one of you might give me your comments on any of these options.

John, do you want to start first?

Mr. **Schnittker**. Yes, I am a little skeptical of amending the Crop Insurance Program to meet an emergency. I think that ought to be viewed in the context of how that might effect the longer-term consideration of crop insurance. We have been working for many years to try to make the Crop Insurance Program a business-like program. Congress and the USDA and commissions are working on this. If we could keep out of crop insurance this year and handle the 1989 drought as an emergency, and amend crop insurance to help handle future emergencies a little better, that might be the best way out.

I believe the right way to proceed would be by analogy with last year's drought. Use that as a pattern, apply it to 1989 Winter wheat, and, if necessary, progressively to the Corn Belt, to Spring wheat areas which are very dry, in case the drought damage falls there.

Mr. **Glickman**. Mr. Berry or Mr. Frey, either one of you?

Mr. **Berry**. I would think that probably I would have to agree with this gentleman on that because you are going to have to change the crop insurance structure of it. It just does not fit to the Winter wheat grower. It kind of penalizes him really and that is my personal opinion.

Mr. **Glickman**. So you would say, if we are going to go with some assistance, we basically take what we did last year and even with the 35-percent threshold at least it is the way it has been applied before and there is a history to it?

Mr. **Berry**. Yes.

Mr. **Glickman**. How about you David, do you have any thoughts on this?

Mr. **Frey**. As a staff member of the Wheat Commission and State agency, we do not take a position on it, because our chairman is involved with the programs and I think would be able to comment as a producer. We also had one comment from one of our other commissioners.

Mr. **Berry**. I might read that to you, Mr. Chairman. This is from Harlan Sloan who is a commissioner also, but speaking as a wheat farmer. He added this comment to his summary and he said, drought relief is a big iffy here in wheat country. He says, Senator Dole said it would be available if needed. It is needed. Hopefully, the drought relief program can be more effective than in 1988. The producer's scenario is he has a wheat crop failure, signs for drought programs and then is fined his regular deficiency payment which is or should be a totally different or separate program.

Mr. **Glickman**. We will consider all of this. Obviously, we have a situation where there are dollars saved. In my judgment I do not want to see OMB take those dollars and stash those away for other purposes. Those dollars are saved because of hardship caused by bad weather. Farmers relied on a program and therefore, I think those dollars need to come back to the producers in as equitable a way as possible.

I guess my only point about the crop insurance issue, and I understand the complexities of all of this, I was one of those who voted to replace the Disaster Program with crop insurance. It was the vote of Mr. Sebelius, who was a member of this committee then and myself who did that, because we thought that in the same way a homeowner or a carowner bought insurance, hoping he would never have to collect on it. It was just insurance. That we could have crop insurance perform the same function and that 9 years out of 10 or 18 years out of 20, you would never collect. It was just a cost of doing business. It would be a reasonable enough rate so that people could afford to do it. And it has not turned out very well.

I suppose that given the fact that the program is being intensively reviewed right now, it would create some complexities to go back and do it retroactively because you would not have dealt with the fundamental underlying problems which, I think, John, was your point.

The other side of the coin is that I do not want people to think that we will always be there for a Disaster Program every year, unless that is our goal. Unless we are going to go back to the Disaster Program. And it may be the experience of all of this is, and I am talking out loud now without being quite sure where I am being lead to which is very dangerous. But it may be the experience of all of this is that we ought to just put the Disaster Program back in the law and have some sort of threshold so that everybody will know automatically what that assistance would be, and not go through this gyration all the time. Because Congress will always want to deal with the hardships out there. I can tell you that right now. Yes, John?

Mr. SCHNITTKER. I hope you will not give up quite yet on crop insurance. My point is that it would be unusual to amend the crop insurance in the next 90 days as an emergency program, but you should keep working on it. And finally, I hope that the committee sometime has taken a look or will take a look at the Western Canadian Income Insurance Plan. It seems to me that that has something to commend itself. It is partly Government supported, partly premium supported and comes in to offset both low yields and low prices. But that again, I would look at for 1991 or 1992, not for 1989.

Mr. GLICKMAN. Your point is not using crop insurance as a 1989 wheat Disaster Assistance Program?

Mr. SCHNITTKER. Because I think crop insurance or income insurance and crop insurance together might still be salvaged as the legitimate long-term programs that you are talking about.

Mr. GLICKMAN. I appreciate all of your testimony, particularly Mr. Frey and Mr. Berry for coming here from Kansas. We will move on something. I can tell you that. We just want to make sure that we know the cost significance of what we are talking about, but as most of my colleagues have said and the same way that we dealt with this problem in one region of the country, I think that most people believe in all fairness that those of us who are in another region who are now suffering ought to have the same benefits. So we will do our best to try and move in that direction. We will let you all know when and if we come up with some sort of decision on this.

Mr. **Frey**. Thank you very much, Mr. Chairman.

Mr. **Glickman**. We appreciate you all coming here. Thank you very much, the hearing is adjourned.

[Whereupon, at 12:03 p.m., the committee was adjourned, subject to the call of the Chair.]

[Material submitted for inclusion in the record follows:]

Statement of Ewen M. Wilson
Assistant Secretary for Economics
U.S. Department of Agriculture
before the
Committee on Agriculture
Subcommittee on Wheat, Soybeans, and Feed Grains
April 6, 1989

Mr. Chairman and Members of the Subcommittee, I appreciate the opportunity to appear at this hearing on wheat. In your letter inviting USDA to this hearing you asked us to discuss, first, the weather outlook; second, the outlook for the winter wheat crop; and, third, implications for the 1990 wheat program, wheat exports, and wheat stocks. With me today is Dr. Norton Strommen, USDA's chief meteorologist and Dr. Keith Collins, Director of our Economic Analysis Staff. With your permission, I will make a brief statement, and then we will respond to your questions.

Weather

Precipitation has been above average this winter in the northern Great Plains, in much of Colorado, and in a broad belt extending from the Ohio River Valley to the southern Mississippi Delta. On the other hand much of western Kansas, eastern Colorado, the Oklahoma/Texas panhandle, and southern Nebraska have had below average precipitation.

Kansas normally receives about 6 inches of precipitation in the months of October through February. Typically, 2.1 inches fall in October, 1.3 inches in November, 0.9 inches in December, 0.7 inches in January, and 0.9 inches in February. This year only 3 inches of precipitation were recorded for all these months, and this combined with wide swings in temperatures have stressed the winter wheat crop in much of Kansas.

Kansas normally gets spring rains of: 1.8 inches in March, 2.5 inches in April, 4.0 inches in May, and 4.1 inches in June. In March this year, precipitation totaled about 1.3 inches. Therefore, good rain in April and May will be critical for development of the hard winter wheat crop in Kansas.

The long-term Palmer Index which measures prolonged and abnormal moisture deficiency or excess, shows that pockets of drought persist from last summer in parts of the western Cornbelt, in parts of the Northern Plains, parts of the far West, and in southeast Texas. Good spring rains will be needed for crop development in these areas. On the other hand, subsoil moisture has been fully recharged in much of the soft red winter wheat area extending from the eastern Cornbelt through the Southeast.

Wheat Outlook

The area of Kansas which received less than 50 percent of normal precipitation from October-February produced about 85 percent of the Kansas wheat crop last year. In a normal year, Kansas accounts for about 35 percent of the nation's hard red winter wheat. Kansas production normally accounts for 23 percent of all winter wheat, or 17 percent of total wheat including spring wheat and durum.

The dryness has caused deterioration of the winter wheat crop from Kansas southward into northern Texas. In addition, sharply fluctuating temperatures in early February may have caused above-average winterkill. The cold outbreak did, however, eliminate insects which had multiplied in the mild, winter weather. Dryness has caused the below average tillering of wheat plants in western Kansas.

Not all of the winter wheat crop has been affected by drought. Near- to above-normal amounts of winter precipitation in much of Texas, Oklahoma, parts of Nebraska, and Colorado have provided more favorable conditions for crop development in those areas. This is also true of the soft red winter wheat areas. Precipitation patterns were favorable across the Delta, and from southern Missouri into Ohio, and rains were timely in the Southeast during the critical tillering stage. In most of the white winter wheat areas of Michigan and the Pacific Northwest precipitation has been adequate to abundant. The hard red winter wheat areas of the northern Great Plains have benefited from good snow cover during the winter season, but sub-soil moisture reserves remain below normal and will require further rain for recharge.

The key to 1989 crop yields will be the timing, amount, and distribution of spring rainfall. At this early stage, an indication of crop conditions is provided by weekly reports of the Department's National Agricultural Statistics Service. On April 3, 70 percent of the Kansas wheat crop was rated poor to very poor and only 11 percent good to excellent. This was the worst rating among the major winter wheat states. A year ago, less than a fourth of the Kansas crop was rated poor to very poor and over half of the crop was rated good to excellent. The condition of the Kansas crop improved this week for the first time since early February. Only 9 percent of the crop was rated very poor on February 6, but the crop deteriorated steadily to 48 percent very poor on March 27. On April 3, 38 percent of the crop was rated very poor.

For the major winter wheat states as a whole, 31 percent of the crop was rated poor to very poor, compared with just 8 percent last year. Only 32 percent of the crop was rated good to excellent, compared with 62 percent last year.

The overall condition of the Kansas crop was rated at 61 percent of "normal" on April 3. Recent history indicates that overall crop conditions of poor to very poor on April 1 result in yields below trend, but the yield loss is uncertain. For example, the Kansas wheat crop was rated at 67 percent of normal on April 1, 1977 and yields turned out to be 5 bushels below trend. In April 1957, the condition of Kansas wheat was reported at 60 percent of normal, but that year yields ended up 4 bushels above trend. Above normal rainfall in March through May saved the crop.

Based upon Kansas precipitation data during the period October through February, this season is the fifth driest since 1931. Records show that in 7 of the 10 driest seasons since 1931, Kansas wheat yields have been below trend.

The 1990 Wheat Program

The public comment period for the 1990 wheat program started last week. Three levels of acreage reduction (ARP) are considered in USDA's preliminary regulatory impact analysis: 10 percent, 5 percent, and 0 percent. It is assumed that 11.5 million base acres of wheat will be enrolled in the long-term CRP by 1990. The target price is assumed to be $4.00 per bushel, and the loan rate $1.95 per bushel--both the minium levels established by law.

This compares with a target price of $4.10 per bushel and a loan rate of $2.06 per bushel this year.

Based on preliminary analysis, the difference between a 0 percent ARP and 10 percent ARP is 175 million bushels production, 75 million bushels exports, and 75 million bushels ending stocks. But, these estimates should be viewed with caution. There is still a great deal of uncertainty associated with estimates of the 1990 crop supply and demand when we do not yet have a good estimate of the 1989 wheat crop.

Back in January, USDA estimated that wheat farmers seeded 54.5 million acres of winter wheat. Last Friday, we published prospective plantings of wheat based on a survey conducted between March 1 and March 15. It appears that the winter wheat acreage will total 54.7 million acres, up 12 percent from a year ago. Durum wheat acreage was put at 3.9 million acres, up 16 percent from 1988, and other spring wheat 15.7 million acres, up 17 percent from last year. Thus, total wheat acreage is estimated at 74.3 million acres, up 13 percent from a year ago.

USDA will issue its first assessment of the 1989 wheat crop on May 11. Mr. Chairman, you asked us to provide an estimate of the wheat crop if adverse weather continues. If yields for Kansas decline from trend by an amount equal to the largest decline ever--10 bushels per acre--and if 19 percent of planted acres are abandoned--the worst in 20 years--then Kansas wheat production could fall to 280 million bushels, 150 million bushels below the level expected under normal conditions. Allowing for some additional loss in surrounding states, this implies a 1989 wheat crop of 2.3 billion bushels. I must emphasize this is not an official USDA projection. You will have to wait until May 11 for that. However, it does provide some perspective if dry conditions prevail.

If the 1989 wheat crop is only 2.3 billion bushels, ending stocks on June 1, 1990 would likely fall below 500 million bushels. Exports would also be down, perhaps below 1.4 billion bushels compared with about 1.5 billion bushels exported this year. Under these circumstances, the lower acreage reduction options for the 1990 crop become more plausible.

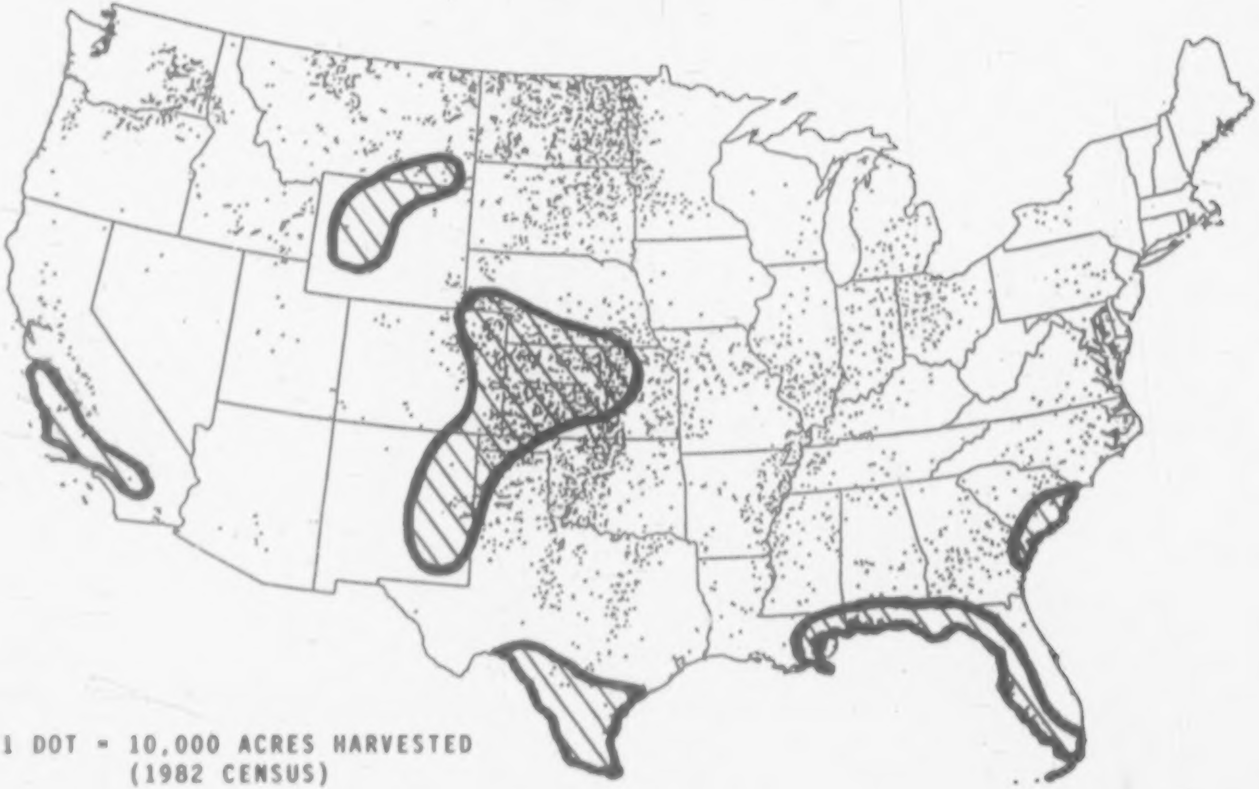
Since the 1990 program does not have to be announced until June 1, there are still 2 months in which to evaluate crop and weather developments before making an acreage reduction decision. As you know, any acreage reduction decision announced by June 1 could still be modified up until July 31 if supply/demand conditions warrant a change. At the present time, prospects for the soft red winter crop appear very favorable, expecially in the Eastern Corn Belt and Southeast. Planting conditions in the Northern Plains are generally favorable for spring wheat and durum.

By June 1, we will know more about the potential size of the 1989 wheat crop and will be in a better position to choose the appropriate acreage reduction program, if any.

That concludes my testimony. I will do my best to respond to any questions you or other Members of the Subcommittee might have.

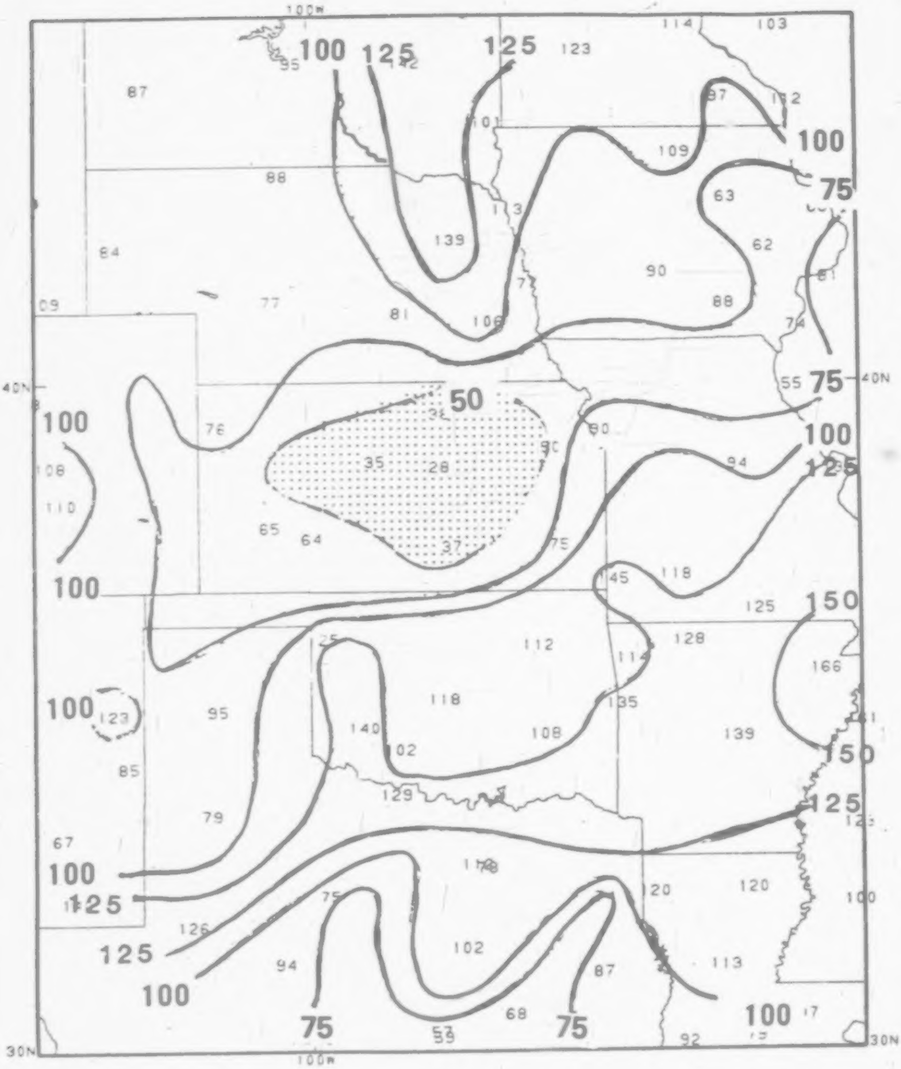
(Attachments follow:)

U.S. WHEAT GROWING AREAS
HATCHED AREAS INDICATE LESS THAN 50% OF
NORMAL PRECIPITATION
1 OCT 88 - 28 FEB 89



1 DOT = 10,000 ACRES HARVESTED
(1982 CENSUS)

SEPT. 1-MARCH 25, 1989 PRECIPITATION, GREAT PLAINS PERCENT OF NORMAL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118
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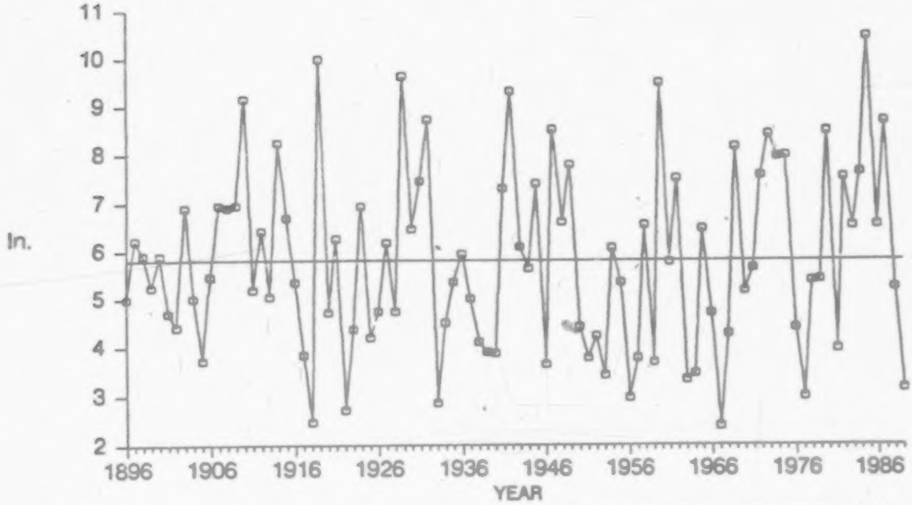
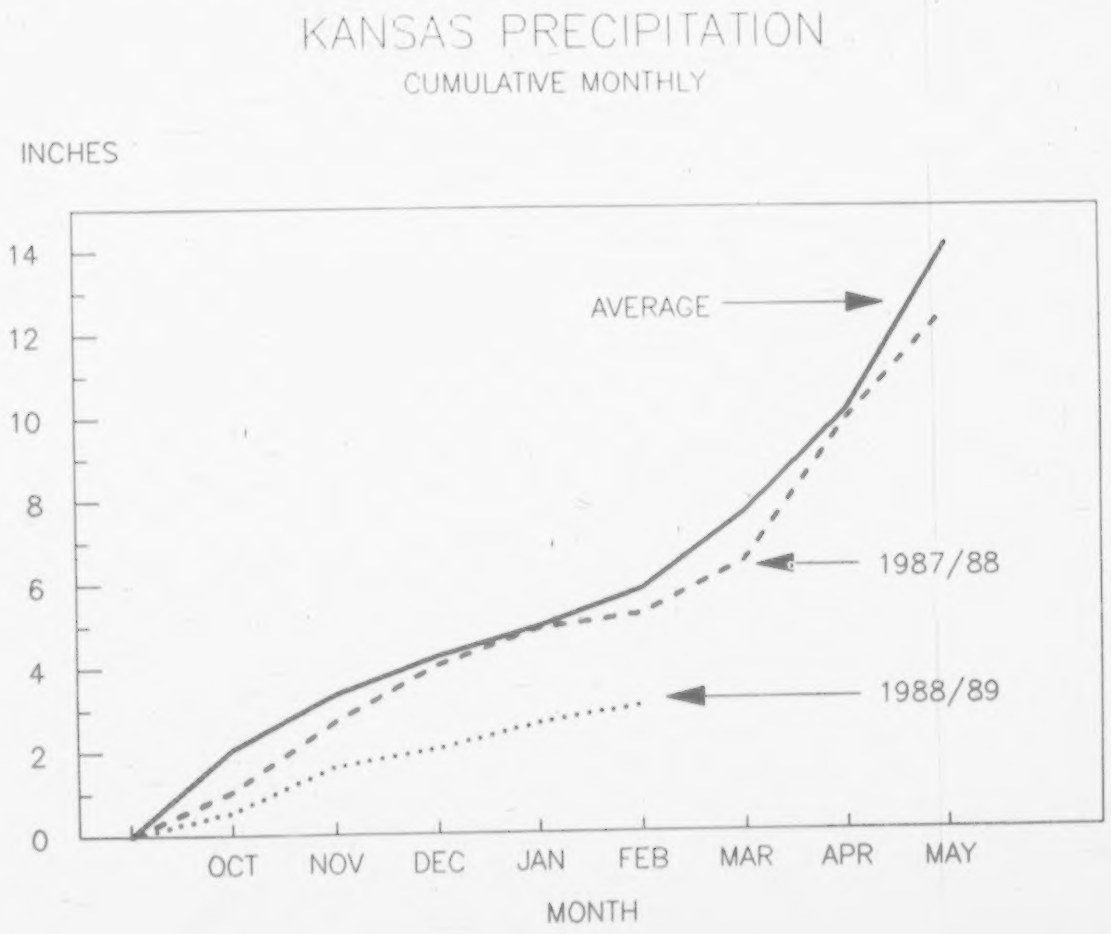
100
30N

OCT.-FEB. PRECIPITATION, KANSAS



National Climatic Data Center, NOAA


KANSAS PRECIPITATION
CUMULATIVE MONTHLY
INCHES
14
12
10
8
6
4
2
0
AVERAGE
1987/88
1988/89
OCT
NOV
DEC
JAN
FEB
MAR
APR
MAY
MONTH

Kansas Monthly Precipitation 1/

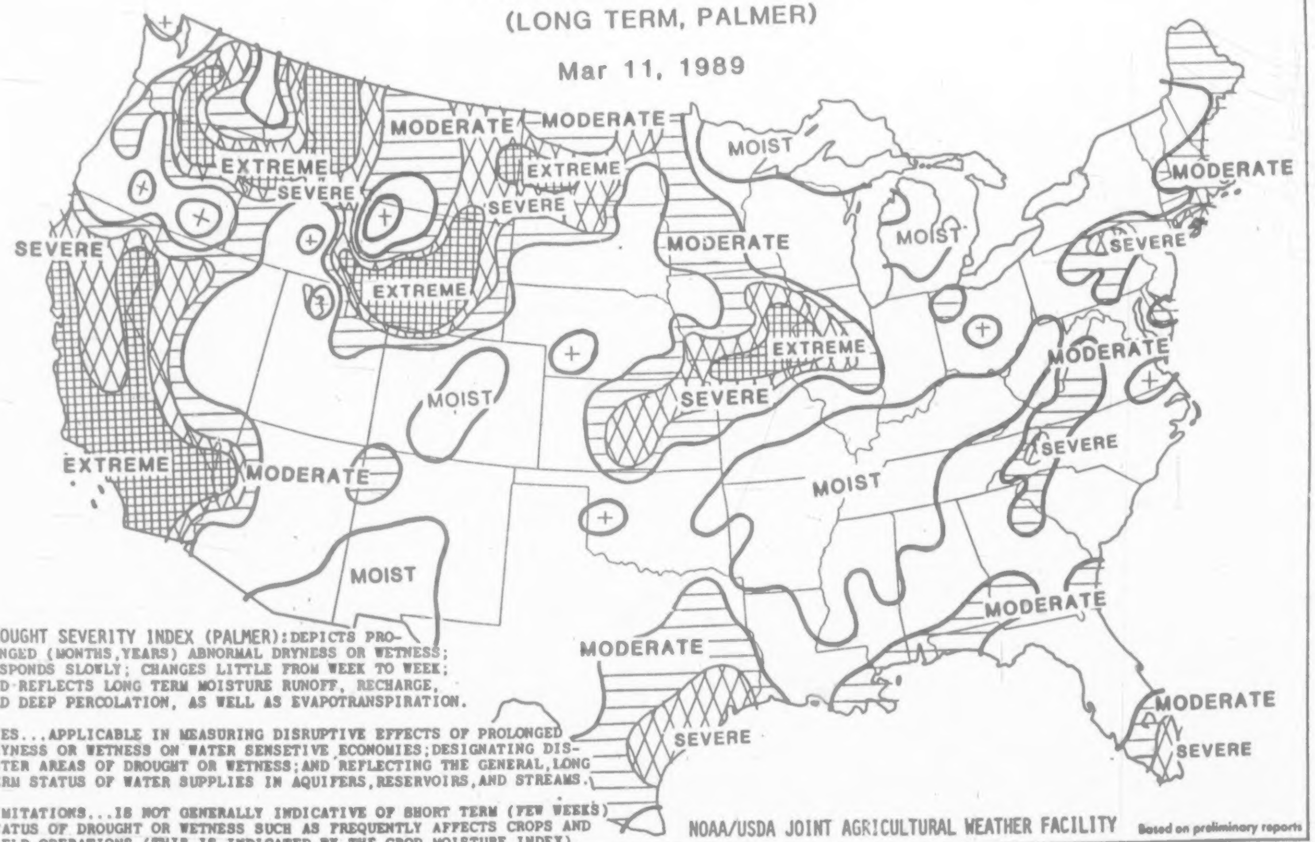
Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Annual
						- - - - - - inches - - - - - - - -							
1987	.83	1.71	4.82	1.72	5.42	4.03	3.24	4.63	2.05	1.07	1.67	1.33	32.52
1988	.84	.34	1.25	3.39	2.61	1.76	3.34	1.80	2.66	.57	1.09	.41	20.08
1989	.57	.43	1.30										
Mean	.71	.86	1.81	2.46	3.96	4.09	3.16	3.06	2.86	2.06	1.31	.89	27.23
SD	.54	.47	1.29	1.23	1.42	1.78	1.72	1.23	1.59	1.28	1.03	.56	5.65
Maximum	3.13	2.12	7.79	7.11	7.61	9.55	8.70	6.53	8.35	5.94	4.26	2.60	41.50
Year	1949	1960	1973	1944	1935	1951	1950	1977	1973	1941	1931	1984	1951
Minimum	.00	.06	.12	.75	.98	.84	.65	1.08	.29	.02	.03	.04	15.39
Year	1986	1963	1936	1963	1966	1952	1935	1936	1956	1952	1954	1976	1956

1/ Mean and minimum and maximum data based upon records beginning January, 1931.

DROUGHT SEVERITY

(LONG TERM, PALMER)

Mar 11, 1989



MODERATE
MODERATE
MOIST
EXTREME
EXTREME
SEVERE
SEVERE
SEVERE
EXTREME
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MODERATE
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MODERATE
SEVERE
MODERATE
MODERATE
SEVERE
+

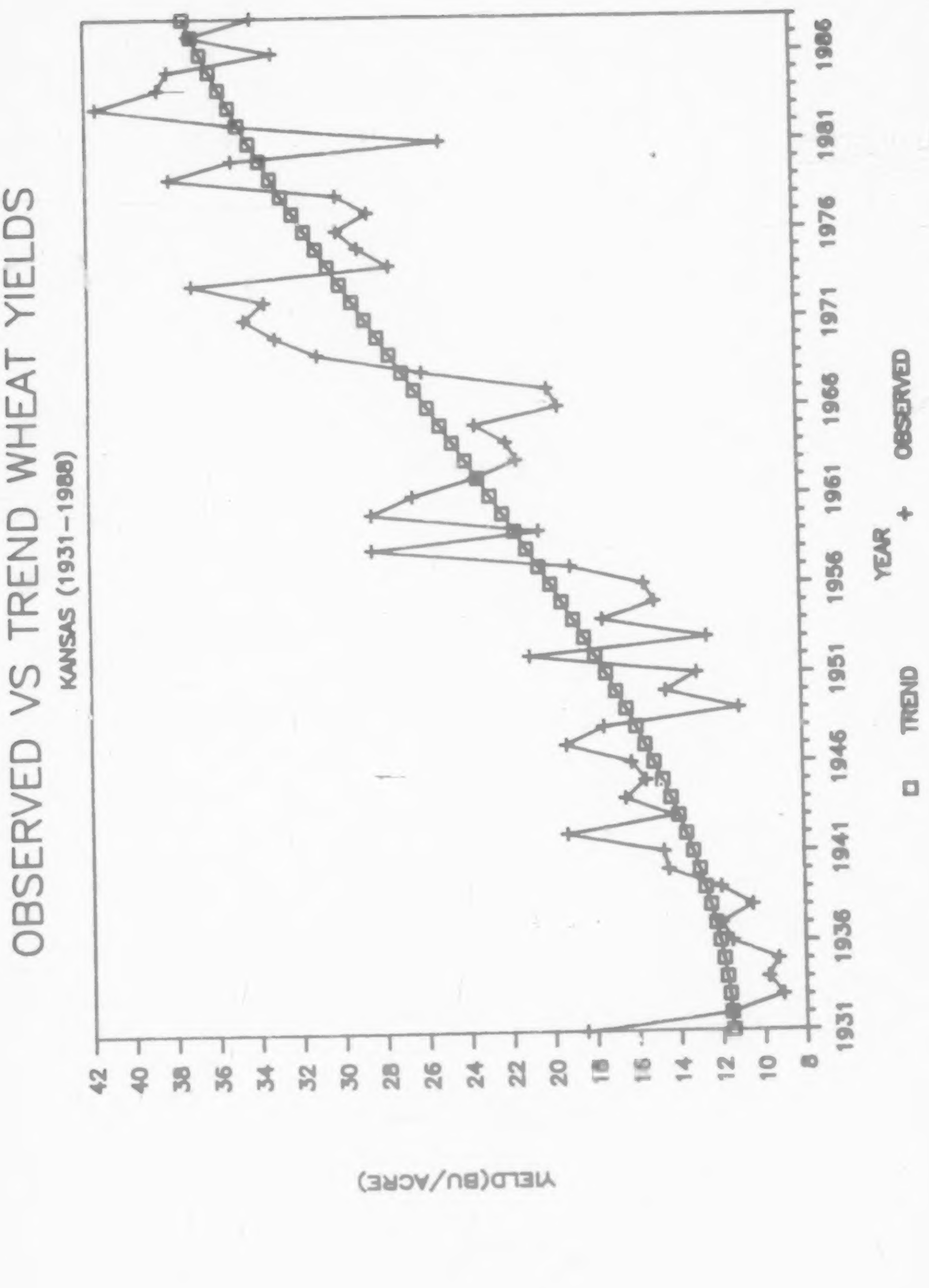
DROUGHT SEVERITY INDEX (PALMER): DEPICTS PROLONGED (MONTHS, YEARS) ABNORMAL DRYNESS OR WETNESS; RESPONDS SLOWLY; CHANGES LITTLE FROM WEEK TO WEEK; AND REFLECTS LONG TERM MOISTURE RUNOFF, RECHARGE, AND DEEP PERCOLATION, AS WELL AS EVAPOTRANSPIRATION.

USES... APPLICABLE IN MEASURING DISRUPTIVE EFFECTS OF PROLONGED DRYNESS OR WETNESS ON WATER SENSETIVE ECONOMIES; DESIGNATING DISASTER AREAS OF DROUGHT OR WETNESS; AND REFLECTING THE GENERAL, LONG TERM STATUS OF WATER SUPPLIES IN AQUIFERS, RESERVOIRS, AND STREAMS.

LIMITATIONS... IS NOT GENERALLY INDICATIVE OF SHORT TERM (FEW WEEKS) STATUS OF DROUGHT OR WETNESS SUCH AS FREQUENTLY AFFECTS CROPS AND FIELD OPERATIONS (THIS IS INDICATED BY THE CROP MOISTURE INDEX).

NOAA/USDA JOINT AGRICULTURAL WEATHER FACILITY

Based on preliminary reports


OBSERVED VS TREND WHEAT YIELDS
KANSAS (1931–1988)
YIELD(BU/ACRE)
42
40
38
36
34
32
30
28
26
24
22
20
18
16
14
12
10
8
1931
1936
1941
1946
1951
1956
1961
1966
1971
1976
1981
1986
YEAR
□ TREND
+ OBSERVED

WINTER WHEAT CONDITION
April 3, 1989

State	Very Poor	Poor	Fair	Good	Excellent
	(percent of crop)				
Arkansas	0	0	10	75	15
California	0	0	5	75	20
Colorado	6	12	54	26	2
Georgia	4	11	51	32	2
Idaho	2	10	35	39	14
Indiana	0	10	47	40	3
Kansas	38	32	19	8	3
Missouri	1	9	40	48	2
Montana	1	13	37	45	4
Nebraska	0	2	80	17	1
New Mexico	30	58	9	3	0
No. Carolina	0	3	16	74	1
Oklahoma	0	10	35	53	2
Oregon	0	1	67	32	0
So. Dakota	2	5	25	60	8
Texas	2	35	50	11	2
Washington	18	44	23	15	0
Weighted Avg.	11	20	37	29	3
Year ago avg. 1/	0	8	30	49	13

1/ Week ending April 10, 1988

COMMODITY FUTURES IMPROVEMENTS ACT OF 1989

THURSDAY, JULY 20, 1989

House of Representatives,
Subcommittee on Conservation,
Credit, and Rural Development,
Committee of Agriculture,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:10 a.m. in room 1300, Longworth House Office Building, Hon. Glenn English (chairman of the subcommittee) presiding.

Present: Representatives Tallon, Penny, Nagle, Harris, Staggers, Sarpalius, Long, Coleman, Morrison, Gunderson, Combest, Grandy, and Holloway.

Also present: Representative E (Kika) de la Garza, chairman of the committee, and Representatives Huckaby, Glickman, and Jontz, members of the committee.

Staff present: Fred J. Clark, associate counsel; William E. O'Conner, Jr., assistant minority staff director; John E. Hogan, minority counsel; Alice Devine, minority associate counsel; Glenda L. Temple, clerk; Bill Cherry, James E. McDonald, James A. Davis, Thomas H. Lederer, and David Ebersole.

OPENING STATEMENT OF HON. GLENN ENGLISH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OKLAHOMA

Mr. English. The committee will come to order.

This is the second day of hearings of the Commodity Futures Improvements Act of 1989. Tuesday's witness list included a wide spectrum of the futures industry but today's list is even wider. It includes a farmer, a floor broker, and representatives of most other parts of the industry. We will change the order of today's witnesses. Late yesterday, officials from the Chicago Board of Trade notified us that Mr. Mahlmann could answer questions about the emergency order involving July soybeans if he could appear after trading in the contract ends in Chicago. Trading ends at noon Chicago time or 1 p.m. here. I know that many members of the subcommittee want to get complete answers instead of the answers they got on Tuesday. So I changed the schedule of witnesses. Mr. Mahlmann will appear this afternoon.

To help members of the subcommittee, we obtained the cash soybean prices from the Agricultural Marketing Service at USDA and arranged them in a table that includes the settlement price at the Chicago Board of Trade. This is included in the material in front of the members. I look forward to hearing today's witnesses.

[The information follows:]

CBT July Settlement and High Cash Market Prices of Soybeans for Selected 1989 Dates (Dollars per Bushel)

1989:	CBT July Settle	Chicago 15 day	Toledo	Minn.	Illinois Process.	Memphis	Kansas City
6/30	7.3500	7.3500	7.3850	7.1450	7.4700	7.3600	7.2500
7/03	7.4050	7.4050	7.4350	7.2050	7.6200	7.4000	7.4650
7/05	7.7650	7.7650	7.7350	7.4850	7.8400	7.7400	7.7200
7/06	7.6500	7.6500	7.6350	7.3750	7.7500	7.6200	7.5900
7/07	7.6650	7.6650	7.6100	7.3600	7.6900	7.6400	7.4500
7/10	7.4350	7.4375	7.3850	7.1050	7.3350	7.3700	7.1300
7/11	7.2600	7.2600	7.2100	6.9450	7.2900	7.2500	7.1000
7/12	6.8650	6.8650	6.7850	6.6350	6.9450	6.7900	6.4300
7/13	6.9750	6.9750	6.9200	6.8100	7.0000	6.9700	7.0500
7/14	7.0350	7.0350	6.9550	6.9525	7.0850	7.1000	7.1300
7/17	6.7750	6.8000	6.7450	6.6725	6.8350	6.8400	6.8350
7/18	6.9550	6.9550	6.9350	6.8200	6.9200	6.9800	6.8400

Mr. English. Now, Mr. Coleman, for any opening remarks.

Mr. Coleman. I have no statement.

Mr. English. Mr. Tallon.

Mr. Tallon. I have nothing, Mr. Chairman.

Mr. English. Mr. Combest.

Mr. Combest. Nothing, Mr. Chairman.

Mr. English. Our first witness today is Mr. Robert D. Josserand, who is president of the National Cattlemen's Association.

Mr. Josserand, if you will come to the witness table we will be happy to receive your testimony. Let me also say that, Mr. Josserand, you and all of our other witnesses today, if you would care to summarize your written testimony, please feel free to do so, and your complete written testimony will be made a part of the record.

STATEMENT OF ROBERT D. JOSSERAND, PRESIDENT, NATIONAL CATTLEMEN'S ASSOCIATION, ACCOMPANIED BY ALAN SOBBA, DIRECTOR, TAX AND CREDIT

Mr. Josserand. Thank you, Mr. Chairman.

As you have said, I am Bob Josserand from Herford, TX. I am a cattle feeder; however, I am here today representing the National Cattlemen's Association. I want you, Mr. Chairman, and the subcommittee to know how much we appreciate the opportunity to express our views on this very critical issue as far as the cattle industry is concerned.

I want to say right up front that our primary working relationship is with the CME. Several years ago, we started a cooperative venture in which our cattlemen were extremely concerned about some of the attitudes toward the CME and some of the things that were happening, and we started a joint project with them that has been very successful, I think. We continue to work with them. We think we have made some significant improvements. I would like also to thank the committee for moving in such a timely manner on House bill 2869.

I am going to be very brief, Mr. Chairman, and I will be very happy to answer any questions the committee might have afterwards. I am going to attempt to summarize. I am going to follow the bill's titles. Title I, limitation on certain trading practices—dual trading. Very simply, the National Cattlemen's Association supports the elimination of dual trading. We do not think under the present monitoring system available on the floor that dual trading is supportable by the exchange and simply because the pit brokers' cards are submitted every 30 minutes and there is absolutely no way to successfully monitor and audit trading.

We would also recommend, Mr. Chairman, that the elimination of dual trading simply be across the board on all commodities. I don't think it's feasible to eliminate dual trading in some pits and not all. We would also like to suggest that the elimination of dual trading would probably do more to restore confidence by the cattle industry in the futures market.

We would also like to support membership disclosure and elimination of dual trading for individual traders in banning members of brokers' associations from trading for their personal accounts in all exchange markets against orders executed by members of the same broker association, regardless of profit-sharing arrangements. Allowing dual trading to continue within broker groups but prohibiting it by individual traders is not fair and would put several people at competitive disadvantage.

Title II, the enhancement of regulatory and enforcement activity—audit trails. One of the great concerns, Mr. Chairman, of our industry is the audit trail. And we do not think today, given the fact that pit broker cards are bracketed into 30-minute segments that the exchange can narrow the audit trail to make it meaningful. We would like to recommend that increased audit procedures to cross-match information on a pit broker's card with the brokerage house, outside orders, be mandatory.

NCA also recommends increased research into the use of hand-held electronic recording devices or other emerging technology to record pit brokers' transactions in lieu of the traditional hand-held pit broker cards. We also support the concept of separate time brackets for market openings and closings. We feel that there is too wide a trading range at the present time and we would like to see a definite time bracket.

Closer and more frequent monitoring of positions held by registered commercial traders is recommended to assure that these positions are in fact bona fide hedged positions. Auditing procedures may be required to establish that the commercial trader in fact has product or orders in the physical market that are being offset by hedged positions in the futures market.

The National Cattlemen's Association has been working quite closely with CFTC Chairman Wendy Gramm; has urged their complete and full cooperation with the ongoing FBI investigation. We continue to participate and cooperate wherever possible so that the public confidence in the integrity of the futures market is maintained.

The National Cattlemen's Association supports the concept of self-regulation by the futures industry with continued strong oversight by CFTC. We feel that if the exchanges themselves will adhere to the penalties as proposed by the exchanges and will continue to monitor their own activities, with oversight by CFTC, that it would be much stronger than additional people, additional regulators from CFTC on the floor or in the pits. Strengthening self-discipline committees will help restore integrity to the market. We would also urge that greater representation by nonfloor membership is a necessary step. One item that we would like to see handled in your bill, if possible, is the fact that we do require registration of floor traders, or require some type of activity which will give cattlemen and others increased confidence in floor brokers.

We also think that tied with the registration of floor traders should be enhancement of registration requirements. We are not sure that we totally have the kind of background checks and education required for brokers. The concept of self-regulation with strong CFTC oversight is supported by NCA. Without strict enforcement of penalties, regulations lack the teeth to insure compliance with self-imposed rules.

The integrity of self-regulation is directly tied to ethical standards. We would urge the committee to make sure that extensive ethical training would be established both for the exchanges and the floor brokers. We would like to share just a few other comments with you, Mr. Chairman.

We would recommend and support permanent authorization of CFTC. We feel that this is long overdue. It would allow the Commission to redirect some of the funds and staff that presently is expended to repair for reauthorization and would allow that staff and funds to be directed towards its primary function.

We think that adequate numbers of highly trained, qualified, experienced personnel are central to the accomplishment of any mission. NCA supports CFTC's request for increased personnel and funding, which have been outstripped by growth in the futures industry during the recent years. One specific issue, periodic verification of positions held by commercial traders as bona fide hedges is the type of information that increased surveillance could create and should create.

The use of electronic systems in place of open outcry offers unlimited advantages in recordkeeping, market surveillance, ease of use, and opens opportunities for additional refinements. NCA strongly encourages the exchange to implement electronic trading systems during normal trading hours as an alternative to open outcry.

We think that, while this is a long process and we appreciate your efforts, we think that what you are doing will restore market integrity in light of the recent investigation by establishing CFTC as the futures regulatory agency, you will serve very much the people in the country.

Mr. Chairman, National Cattlemen is certainly willing to assist you in any way that we can in this endeavor and I would be happy to answer any questions should there be some.

Thank you.

[The prepared statement of Mr. Josserand appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Mr. Josserand. I appreciate that.

Let me ask you with regard to the state of confidence in the futures markets as far as the cattlemen of this country are concerned, members of your association. Do they have a high level of confidence in the integrity of the market as it stands today?

Mr. JOSSERAND. Mr. Chairman, I would have to say that certainly the opinions are split. If you asked me for a percentage, I would say probably half of our members do have that confidence; half have some concern, particularly those who do not use the futures as a price risk protection mechanism, those who—I do not want this to sound wrong—but those who are in rural areas that just simply do not have adequate communication on a daily basis; I think those people have some concern about the integrity of the market.

Mr. ENGLISH. We heard a great deal of concern expressed, of course, from the industry itself shortly after it was announced in January that there had been a probe by the Justice Department, that an undercover operation had been under way for several months; and we seemed to find a great deal of interest within the industry in trying to address any problems pertaining to questions of the integrity of the market, to be willing to tighten up. As time has gone by and no one has been prosecuted; that seems to be lessening. Does that change anything, the fact that no one has been indicted and prosecuted to date? Does that change the need, in your opinion, for addressing the question of integrity?

Mr. JOSSERAND. Absolutely not, Mr. Chairman. In fact, I think it intensifies that need from the standpoint that in the country, the general feeling is, you know, the investigation was announced, that there would be indictments forthcoming and, as you say, nothing has occurred. I think the country is saying why, when, and what are we going to do about it; and I think if anything it intensifies the efforts on your part.

Mr. ENGLISH. Mr. Coleman.

Mr. COLEMAN. Well, Mr. Josserand, your organization and the Chicago Mercantile Exchange have entered into some advisory capacity; there's an advisory board and so forth. Would you tell us a little bit about the ongoing relationship that you all have set up and how do you think those are proceeding?

Mr. JOSSERAND. Yes, sir, Mr. Coleman. We have had in the past 2 years a very good working relationship with the Chicago Mercantile Exchange in that our members asked 3 years ago for a task force to be appointed out of the National Cattlemen to really take a look at the cattle futures and what they meant to the industry; and within the framework of that task force and in the framework of the recommendations that came out of that task force, we feel like we have been at least partially responsible for some significant changes in the cattle futures; we feel like that we have had some input and we do have nonvoting members serving on the live cattle committee and the advisory committee; we do feel like we've had a considerable amount of input into some significant changes, important changes as far as we were concerned. We have not gotten all of the things that we thought would make the cattle futures a better tool for us, items such as cash settlement, which we would still like to see.

We also realize the difficulty in the use of cash settlements because of our pricing situation within the entire industry. We still feel that that is a viable option down the road, but we also realize that the industry has to solve its own price discovery system.

Our relationship with the Merc, I submit to you, is very good; they have been very cooperative; we've worked with them. We still have some changes we would like to see made, but I think that's possible, and I think they are open to input from the cattlemen.

Mr. COLEMAN. Well, I thank you.

Mr. ENGLISH. Mr. Tallon.

Mr. TALLON. Mr. Chairman, thank you, and Mr. Josserand, thank you for your testimony.

In looking back over it, of course, we heard you testify that you support elimination of dual trading, period. Of course, the legislation, the bill that has been introduced provides for dual trading under certain circumstances. How would you feel if we included in this legislation criminal penalties, if we provided for criminal penalties within the legislation for a trader that was trading ahead of the customer? Do you feel like that should be included in the legislation?

Mr. JOSSERAND. I think, Mr. Tallon, if you asked our members, the integrity of the exchanges is foremost and I think that our membership would have no problem with that type of activity.

Mr. TALLON. Thank you.

You seem to indicate the problem that you have with dual trading is with the way the audit trail is reconstructed. At the present time, is there a possibility that with a tighter audit trail, a more efficient audit trail that you could be confident with dual trading? What kind of changes would you recommend?

Mr. JOSSERAND. I think No. 1 is that we do have to tighten up the audit trail. I think our concern is simply the integrity when we have dual trading and under present circumstances, I guess our best option is the total elimination of dual trading. If, in fact, we were comfortable and the country was comfortable with the audit trail, then I think we might reconsider that.

Mr. TALLON. I think you said that maybe half of your members had a problem with dual trading, and maybe the other half did not, and that probably the half that did not were people who didn't use the market on an ongoing basis and maybe were not as close to the market and maybe didn't communicate or have the means of communicating with the markets?

Mr. JOSSERAND. Mr. Tallon, what I think I said or hope I said was that with regard to the futures market, about half of our members had real questions about the use of them. I think as far as the dual trading goes, you could say almost 100 percent of our membership would recommend the elimination of dual trading under present auditing procedures.

Mr. TALLON. And so the recommendation certainly would extend to a ban on all dual trading, regardless of the amount of volume in contracts, no concern for liquidity; I mean, we just ought to ban dual trading across the board?

Mr. JOSSERAND. Mr. Tallon, we are very sympathetic to what the ban on dual trading would do to liquidity in a particular contract. We realize that there possibly can be some serious repercussions. However, we think if we do not get the elimination of dual trading, the repercussions from the questioning of the exchange and the futures contract greatly outweigh the lost liquidity.

Mr. TALLON. Of course, we all understand there is nothing wrong per se with dual trading; it's trading ahead of the customer, trading your own order before the customer's order, that's the real problem here, and in my mind, another concern that I have that we've heard really very little about is when a futures merchant gets an order, before it ever gets to the floor of the exchange, we are very limited in how we monitor what happens to that order or those orders, or those bundles of orders.

Has the National Cattlemen's Association looked at that and do you have concerns about how those orders are handled?

Mr. JOSSERAND. I'm sure that our task force, working with the CME, did look at that, Mr. Tallon, but I am not knowledgeable about that.

Mr. TALLON. Well, you understand that you can ban dual trading on the floor, but there are so many things that can happen prior to that order ever getting to the floor; and I just have to question if maybe we can't see the forest for the trees.

Thank you.

Mr. **Josserand**. Thank you, sir.

Mr. **English**. Mr. Combest.

Mr. **Combest**. Thank you, Mr. Chairman.

Mr. Chairman, Mr. Josserand is a constituent of mine and only at the last moment yesterday did he find out he would be delivering this testimony. I know how anxious he is, as soon as he leaves here, to get back to West Texas, and from a personal experience of both of us loving West Texas, far be it from me to be the one that would keep him from it. I have no questions. Bob, it was good to see you.

Mr. **Josserand**. Thank you, Mr. Congressman.

Mr. **English**. Ms. Long.

Ms. **Long**. Thank you, Mr. Chairman.

It's nice to have you here today.

You have been talking about liquidity and dual trading and I think that I am sensing from your—you haven't said this specifically—that the dual trading leads to liquidity, which leads to greater market volatility, because you have people buying commodities that you have no real use for in your case, cattle, their buying cattle to resell and that's in a sense playing with the true forces of the market. Is that what you are saying?

Mr. **Josserand**. Well, I think our concern about dual trading is one of fairness, one of the integrity of the market. I guess if you looked at the cattlemen in general, there are those who do have that concern about people trading in any futures market without need of the product; but at this point in time, a discussion on dual trading I think is one of fairness and is one of perception as much as anything that things are being handled correctly and right and that there is not misuse of the ability to dual trade.

I think more than anything I have to say that with the confidence in the system, I think it's perception more than anything else.

Ms. **Long**. Let me ask you another question along those same lines. We tend to assume that liquidity is in and of itself good because it can keep a market active. Are you suggesting that liquidity has some negative aspects, that liquidity that results from demand from buyers who have no real use for the commodity that that is not necessarily good for the market?

Mr. **Josserand**. Ms. Long, I am not trying to say one way or the other.

I think as far as the position of the National Cattlemen, we certainly would encourage all of the liquidity we could get into a market, even though we realize that it can cause some wild price fluctuations once in a while. I think if you analyzed our membership and particularly that segment which probably are not familiar with the futures, you would find that they would be quite consistent with the idea that maybe there is too much liquidity once in a while.

Ms. **Long**. Thank you. I'm trying to, the same as you, I think, assess the value of liquidity in the marketplace and am glad to have your input. Thank you.

Mr. **Josserand**. Thank you.

Mr. **English**. Mr. Harris.

Mr. HARRIS. Thank you, Mr. Chairman.

One of the complaints or observations that I've had expressed to me concerning the ban of dual trading is that this would drive the markets overseas, and I just wondered if you have any thoughts on that?

Mr. JOSSERAND. No, sir.

Mr. HARRIS. Because we certainly don't want to send any more jobs overseas than we have already seen go. We would like to get some back.

Mr. JOSSERAND. No, sir, I do not have any thoughts on that, and I'm sure it has been looked at by our task force. I simply cannot answer that. I do not know.

Mr. HARRIS. You would agree with me that that is a concern?

Mr. JOSSERAND. I would agree with you that we don't need to transfer a lot more of our business overseas; yes, sir.

Mr. HARRIS. That's all I have, Mr. Chairman. It's good to see you again.

Mr. ENGLISH. Thank you very much, Mr. Harris.

Mr. Josserand, we appreciate your testimony very much.

Mr. JOSSERAND. Thank you, Mr. Chairman.

Mr. ENGLISH. Did you have a question, Mr. Coleman?

Mr. COLEMAN. If I might just make a comment as a followup to my colleague's question, on the other hand, if dual trading were prohibited under certain circumstances, the integrity of the markets in this country would be unquestioned, any problems that might result from dual trading could be caught in a proper audit trail under our proposal. When they exist for higher traded volume, just the opposite probably would occur, would it not? The people who want to buy and sell cattle would want to come to the United States, to make sure that they knew they were getting the proper price and that there was no one taking advantage of their position and so forth. So I would suggest that the bill and the thrust of the bill would be very supportive of trying to retain and enhance our markets as opposed to somehow driving your membership, for example, away from our markets.

Mr. JOSSERAND. I think you are right, Mr. Coleman. I cannot perceive of it happening any other way.

Mr. COLEMAN. Thank you.

Mr. ENGLISH. Thank you very much.

Mr. Josserand, we appreciate your testimony.

Mr. JOSSERAND. Thank you, Mr. Chairman.

Mr. ENGLISH. Our next witness is Mr. Leo Melamed, who is chairman of the executive committee and special counsel to the board, Chicago Mercantile Exchange in Chicago, and I believe he is going to be accompanied by Mr. William Brodsky, president and chief executive officer, and I believe Mr. Jerrold Salzman will also, outside counsel, will be accompanying him as well.

Leo, we want to welcome you here today and we appreciate you coming down and testifying on this legislation. We are looking forward to hearing your views.

STATEMENT OF LEO MELAMED, CHAIRMAN OF THE EXECUTIVE COMMITTEE AND SPECIAL COUNSEL TO THE BOARD, CHICAGO MERCANTILE EXCHANGE, ACCOMPANIED BY WILLIAM J. BRODSKY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, AND JERROLD E. SALZMAN, OUTSIDE COUNSEL

Mr. **Melamed**. Thank you, Mr. Chairman and members of the subcommittee. I am pleased to be here and honored to represent the Chicago Mercantile Exchange. I am here today with our president, Mr. Brodsky, and general counsel, Mr. Salzman.

I have extensive written testimony, Mr. Chairman, that I would like to submit for the record. At this time, I merely would like to make some opening remarks.

Mr. **English**. Without objection, so ordered.

Mr. **Melamed**. Thank you.

Mr. Chairman, I wish to compliment you and the members of this subcommittee on the investigative effort you have undertaken. It is critical to the future of a very important industry. You should recognize that the expeditious and forthright manner in which you conducted the inquiry serves our industry very, very well.

I am pleased that whatever help we were able to give you in the process brought the investigation to a very expeditious point as we sit here today. I suggest that we move forward from here with a legislative result and reauthorization.

I thank you for undertaking this effort in the manner you did.

I would like to offer a little historical overview on the Chicago Mercantile Exchange because sometimes it gets lost in the shuffle. It was on the floor of our exchange some 25 to 27 years ago when this industry expanded in the direction that brought it prominence and importance—financial futures.

Such instruments as futures contracts on foreign currencies, Eurodollars and Treasury-bills were created as a result of inventive genius on the floor of our exchange. Those financial futures later were so successful that they transformed our entire industry. That led to instruments such as U.S. bonds futures, invented at the Chicago Board of Trade and other financial futures contracts the world over. The base of agriculture, which was the reason for these markets in the first instance—and still is today—was expanded into finance. It became so coveted an idea that every financial center in the world today would like a piece of that action that American genius invented. We are very proud of that, as you are.

After the 1987 stock market crash, there was a cry in the financial community that perhaps our futures markets might have been a factor in that crash. And when we testified before Congress on this issue, we urged Congress not to do anything that might injure this American resource. We cautioned that if they did, the American financial fabric could be hurt in the process.

Indeed, there were those who wanted to wrest jurisdiction from the Agriculture Committee and place it elsewhere. And we testified and urged the Congress not to do so.

We were right. Today's hearing is evidence of our view, because this committee has the expertise, the knowledge, the history of the importance of our markets in the national economy.

So, as we come before you today, I present that bit of history. I am proud to be here and to be with you in an effort to make our markets better, to serve not just the national interest but the world interest. We are a world market today, and everyone comes to our doorstep. We want to provide liquid and efficient markets so that no other markets in the world can wrest this American invention away from us.

I thank you, Mr. Chairman, for these brief opening remarks. I am prepared to answer any questions you have.

[The prepared statement of Mr. Melamed appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Mr. Melamed, and I appreciate your statement. I want to recognize the chairman of the full committee, Chairman de la Garza, who has joined us.

Mr. Chairman, do you have any comments that you would care to make, or would you care to lead us off in the questioning?

REMARKS OF HON. E (KIKA) de la GARZA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS

The CHAIRMAN. Mr. Chairman, just very briefly, I want to commend you and members of the subcommittee for the very efficient, practical, and fair way that you have conducted the hearings on the reauthorization of the CFTC and all of the other issues that are before you.

I want to very much extend my appreciation to the industry for the manner in which they have cooperated with us without exception, all segments of the industry. Your responsibility is to those that you serve. We appreciate that. Our responsibility is to those that we serve, including you and those you serve. So, we have a mutual interest in seeing that the industry works hand-in-hand with us for the farmers and all that benefit from what you do.

I wish to thank the industry for the excellent way they have cooperated with us. I will leave the time for questions to the rest of the members of the subcommittee, Mr. Chairman.

Thank you very much.

Mr. ENGLISH. Thank you, Mr. Chairman. We appreciate it very much.

Let me say, as we begin the questions, Leo, I do not suppose there is anyone in the industry that is regarded with more respect as far as being a leader in innovation and a leader as far as the best interest of the futures industry is concerned than you are. I think your reputation is well known.

But I would like to read a little paragraph to you, a paragraph that I know you are very familiar with because in a sense you wear two hats. You wear the hat from the standpoint of doing what is in the best interest of the futures industry and looking to the future as to how we can best approach the problems that the industry may have and, at the same time, you wear the hat of representing the Chicago Mercantile Exchange, and most times those hats coincide and fit together very well.

In this particular instance, the paragraph I want to point out was contained in a report from the Chicago Mercantile Exchange, and this was issued on Wednesday, April 19, of this year. It is a report of the special committee to review the trading practices of the board of governors, and it is signed by a very distinguished group, of course including yourself, people who are highly respected including a former Chairman of the Commodity Futures Trading Commission.

It talks about the issue of dual trading, which I think we have had a great deal of discussion about, and it goes through with regard to the rationale for the position that was taken by this committee.

It states that, while it is valid—the good points for dual trading, it has become painfully evident that the public image of the futures markets and their members has been adversely impacted by the widely held belief that dual trading in the futures leads to customer abuses. All past efforts to explain the rationale for the CME's continued acceptance of dual trading have proved ineffective. Moreover, it has been argued that, as the transaction volume grew, in the CME's major markets the need for dual trading to provide liquidity in those major markets became a less important consideration.

This was the justification for the proposal for a ban on dual trading. And I wanted to point this out because again I think it was a very responsible act. I think that the committee put this together and made an excellent recommendation, and also that the provisions dealing with dual trading contained in the legislation before us here today were in fact modeled after those very recommendations by the CME as is the case with regard to some of the other features. Broker associations, for instance, is almost lifted directly from the Chicago Mercantile Exchange.

So, that along with the fact that in some exchanges, there are some contracts, the Standard and Poor's 500 contract that is traded with CME, already contains a version of a ban. I believe 90 percent of the trades that take place in that contract, dual trading is banned, which is very close to what the estimate is as to what this legislation would be as far as industrywide.

So, I guess that I was struck by the fact, on the one hand, it seems that you are moving in a different direction than this committee reported, which you will remember in which you signed off on, on April 19.

Would it be fair to say today that you are representing the Chicago Mercantile Exchange?

Mr. MELAMED. That is correct.

Mr. ENGLISH. And would it also be fair to say that the statements that were made on April 19 were done by people who were extremely knowledgeable in industry, people who certainly had the best interest of the industry at heart, people who certainly would not take any action whatsoever that would be harmful to the futures industry and what we are looking to forward in the future?

Mr. MELAMED. Absolutely correct.

Mr. ENGLISH. And let me also say that the question of driving business offshore—this has been raised a couple or three times—it would seem to me that the United States, as it stands now, certainly with the exchanges that we have, all the exchanges I am speaking of, and with the regulations, with the systems that we have, the big selling point that the United States has and what is, I think, a strong case that can be made for attracting business to the United States is the fact that we do protect the customer.

He is sure that he is going to be treated fairly, and that that integrity itself is a very, very big selling point. And anything that strengthens that integrity and allows us to point to higher standards, even gives us a better case to be made, as opposed to driving business offshore. Would you agree with that?

Mr. **MELAMED**. I would agree.

Mr. **ENGLISH**. Mr. Coleman.

Mr. **COLEMAN**. I, too, Leo, would thank you and the Merc for your constructive proposals. And I think of all the players in the futures market, you all have responded in a very credible fashion. And as the chairman has indicated, we have based some of our legislation on the concepts and the recommendations of your blue-ribbon committee. At that time, they were only recommendations from your committee, but they seemed to be closing some of the gaps.

I think that you recognize, that the board recognizes that credibility is the issue here, and that we do not want anybody to question the integrity or the credibility of these markets. We do not want to drive people overseas. We want to retain them. We want them to grow and prosper but within a context and framework so everybody knows that what is happening is aboveboard, proper and appropriate.

Having said that, you still differ with us to a certain extent on the dual trading aspect. Your proposal is not exactly identical to the one we have in the bill. And it is based upon an accuracy record of 90 percent, I believe. Once you get to that level and verify that level your proposal would allow dual trading to occur. Is that basically correct, with some exceptions?

Mr. **MELAMED**. That is right.

Mr. **COLEMAN**. What is the current accuracy record on your exchange?

Mr. **MELAMED**. It averages approximately 85 percent exchangewide.

Mr. **COLEMAN**. And how does that relate to 5 or 10 years ago?

Mr. **MELAMED**. It is exceedingly better than it was 10 years ago. We did not have a CTR system to measure that accuracy rate. CTR, as you know, is a result of a lot of work between the Chicago Board of Trade and Chicago Mercantile Exchange. It was implemented at the behest of the CFTC about 2 years ago and has been given great credit because no other exchanges in the world—not even the security exchanges—have a system that is as efficient and as up-to-date as CTR.

It can be made better and, obviously, that is our goal.

Mr. **COLEMAN**. Does the CFTC have a standard that it has given you or goal to reach within a certain period of time?

Mr. **MELAMED**. I do not know that we are on a set standard. I think 90 percent has been sort of a general goal that the industry and the CFTC would like to strive for.

Mr. **COLEMAN**. Mr. Salzman, do you want to comment? Do you know the answer to that question?

Mr. **SALZMAN**. Ninety percent, I believe.

Mr. Coleman. I asked this of Chairman Gramm. The rule the Commission is under is 100 percent accuracy, but nobody has attained that. Is that true? Is that your understanding?

Mr. Melamed. Not my understanding. My understanding is that the goal had been from the inception that about 90 percent was a reasonable level of expectation that would give everyone the comfort level they are trying to achieve; 100 percent is difficult unless your trade is done on a computer.

As you know, we have plans for an after-hours electronic transaction system that would indeed track an audit trail at 100 percent, but that is without human beings. There are no human beings that can effectively do anything at the 100-percent level; but computers can.

In electronic after-hours trading we expect the audit trail to be exactly what you suggest.

Mr. Salzman. I would just like to add, the standard that we are looking at is 90 percent verifiably accurate. That does not mean that we are not 100 percent accurate. It means that there are certain times assigned to trades that cannot be proved through other evidence to be correct.

We think that a very substantial percentage of those trades that are not "verifiably" accurate are accurately timed.

Mr. Coleman. What would be those types of trades?

Mr. Salzman. They would be trades where two or three prices may have occurred within a short period of time, and where we do not have a time stamp on one piece of paper that absolutely shows that the trade was done at time one rather than time two, but we have other reasons to be confident that it was done at time one rather than time two. We do not count that as verifiably accurate.

Mr. Coleman. Now our standard to allow dual trading is pretty well set forth in the exemption which says that an audit trail would have to be capable of detecting any and all trading violations and is fully verifiable. How does that differ from your proposal?

Mr. Melamed. Well, fully verifiable is what I was referring to as a very difficult standard to achieve. While we expect that all systems can do better, no systems will ever be perfect. So, what we are suggesting is that we are going to try to achieve a 90 percent verifiable standard. At that point in time, we will have a comfort level that ought to satisfy all reasonable requests in terms of verifiability.

Mr. Coleman. Can I go on, Mr. Chairman, or do you want to go around again?

Mr. English. I think without question, we are going to go around again because I have some additional questions. I am sure other members will afterward.

Mr. Tallon.

Mr. Tallon. Mr. Chairman, thank you. And, Leo, thank you for your testimony.

I think you said that your accuracy of your audit trail is about 85 percent overall average in all contracts. How long do you think it would take you to reach 90 percent accuracy with the technology? I mean, you would have to spend more money, I would assume, on technology.

Could that be done in 12 months, 15 months?

Mr. **Melamed**. Well, I believe we can do it rather quickly. I would not want to label it within a couple of months, nor are we talking in terms of many years. Some time within 1 year it can be done, probably substantially less than 1 year.

The way to do it though is not just to throw money at it. Many of the reforms that were suggested by the Special Committee To Review Trading Practices that Chairman English has made reference to, are the reforms that have to be adopted—the hourly pick up of the trading cards, special brackets at the opening and at the close, lowering the half-hour bracket to a smaller increment of time like 15 minutes.

With few exceptions, the reforms recommended by the special panel have been adopted by our board. These reforms will serve to increase accuracy of the audit trail.

Mr. **Tallon**. Leo, would the system you have and improvements in the system you have and doing everything you can do, how difficult is it going to be to meet this bill's requirement of detecting any and all of these? Can you do it?

Mr. **Melamed**. Any and all, I do not think so. If you had 100 percent verifiability, you would not detect any and all abuses because people are people. I do not know of a system yet devised, in any industry, anywhere in the world that can detect all abuses.

I do not believe our system and the people who work within it are worse than anybody else, but I do not think you can detect 100 percent of anything anywhere.

Mr. **Coleman**. Where is dual trading banned in exchanges that you would be competing with around the world?

Mr. **Melamed**. There is hardly any ban on dual trading in the United States or world financial markets. In the securities market there certainly is no ban—the specialists on the New York Stock Exchange are dual traders. The financial manager in cash markets, be it currencies or be it bonds, be it any cash market, is a dual trader.

I dare say that is true in the agricultural industry as well. It is certainly true throughout the world in all the forms and in all the financial centers and all the futures exchanges. Throughout the world there is a form of dual trading. It is not banned.

Now it is not always the same, but it is not banned.

Mr. **Tallon**. Leo, the specialists on the New York Stock Exchange, those dual traders, how many of them are there?

Mr. **Melamed**. Mr. Brodsky.

Mr. **Brodsky**. I, of course, cannot speak for the New York Stock Exchange, but basically on the New York Stock Exchange there are about 1,300 members, and I would guess there are probably about 500 members who are engaged full time as specialists. Again, I am giving you an estimate.

Of course, what is significant about the New York Stock Exchange's system is that a specialist has the sole franchise to trade a particular product, where in our markets there is competition between floor traders and among floor traders. So, there are significant differences, but in the particular case of the New York Stock Exchange, the specialist maintains the only public limit order book, and has access to that book, and also has the right to trade for his own account.

Of course, this has been a subject of review by other congressional committees for many decades.

Mr. **Tallon**. And how many traders, how many seats do you all have on the Chicago Mercantile Exchange?

Mr. **Brodsky**. We have approximately 2,700 seats on our exchange. So we have more than double the amount on the New York Stock Exchange.

Mr. **Tallon**. And of those 2,700, do you have any idea how many of those people or what percentage of them are in dual trade?

Mr. **Melamed**. I would say we are talking about in the nature of maybe 33, 40 percent.

Mr. **Tallon**. So 40 percent of 2,700, you have certainly got a lot more specialists.

Mr. **Melamed**. I might be too high. It might be a lot less than that. We have never taken the actual count. So, the range of 40 percent might be far too high. It might be down to, say, 25 percent, in that area.

Mr. **Tallon**. Well, today, if all of a sudden at 11 o'clock this morning, none of those 2,700 floor brokers were allowed to dual trade anymore, what kind of impact do you think it might have on liquidity on your exchange?

Mr. **Melamed**. Well, that is the $64,000 question. I am afraid that it is very difficult to answer except to say it would be dangerous because dual traders provide a form of liquidity in certain pits. Depending on the nature of the market, they provide a mainstay of liquidity. It is not even. I mean there are some markets that need it more than others.

But that is the danger in this delicate balance between the perceived evil that dual trading might represent, which is a perception, and the reality of the liquidity they do provide, which is reality. And in trying to balance the two, we are always very mindful of the fact that if we go too much to one direction, we hurt the other direction. You are talking perception versus reality.

Your question is right on the button, very important. I cannot answer the question but to say that it is a dangerous kind of situation. We must be very careful not to injure whatever liquidity that is provided by those traders.

Mr. **Tallon**. It might even possibly be catastrophic. If nobody were allowed at 11 o'clock this morning to dual trade anymore, the spread could become impossible and there would be no more liquidity.

Mr. **Melamed**. I would not rule that out. That is one of the dangers that we are dealing with absolutely.

Mr. **Tallon**. Thank you. My time has expired, Mr. Chairman.

Mr. **English**. Mr. Combest.

Mr. **Combest**. Thank you, Mr. Chairman.

Mr. Melamed, I need to replow a little ground here, and I apologize to my colleagues if I am the only one that is a little fuzzy on this, but I need to try to make sure I am clear on what you are saying.

In your testimony on page 18, reference to any and all instances of trading violations and the requirements that the audit trail be fully verifiable, you say these are impossible standards. Perfection is not attainable in the futures industry nor in any other. Detection of any and all instances of wrong-doing is an unreasonable standard that can never be met.

Yet, I thought I heard you define that probability of reaching that as very difficult in a question to Mr. Coleman.

Let me make it for sure. Is your testimony that you are saying that detection of any and all and the fully verifiable are impossible, you cannot attain it ever, period? Is that right?

Mr. MELAMED. In the environment of open outcry, when humans are the element being used to create the transaction, I am saying yes to your question. It is impossible.

If you are talking about the electronic or technological world such as with computers, such as we are also suggesting to create, it is not impossible. In fact, we will attain it.

Mr. COMBEST. It was suggested by someone—and I apologize I cannot recall who; I do not guess it really matters—that that technology is available today.

Mr. MELAMED. In terms of computers, it is, yes. And we will use it.

Mr. COMBEST. In follow-up to the chairman's initial questioning, I want to be sure I am also clear on this issue, are you saying that you would not be concerned—are you saying that if the bill in its current form passes and becomes law, that you would not be concerned about any loss of business offshore?

Mr. MELAMED. No, I am not saying that.

If the bill passes in its current form and if we cannot comply with the requirements and the standards set and if, in fact, we have taken away dual trading capability from a large segment of our market participants, I am very much concerned with what will happen to liquidity.

Our competitors are now worldwide as I said in the opening remarks. The Japanese just this June opened a market directly in competition with the inventions of the Chicago Mercantile Exchange. As you know, the Japanese are very competent in what they do.

I am very concerned that they can and will attempt to wrest these markets from us. I am not at all saying that they cannot. Even standing with us toe to toe, without any restrictions on our market, it is going to be a difficult battle as it is. With restrictions that might injure the liquidity base of our markets, then I say one of our hands is going to be tied behind our back. I do not want to go into that kind of fight, and I know Congress would not want us to.

Mr. COMBEST. One of the caveats you said where you would be concerned about loss of business was if we could not comply. If the bill passes in its current form, do you think that it is possible for you to comply with it?

Mr. MELAMED. Not with 100 percent.

Mr. COMBEST. Thank you.

Mr. ENGLISH. Ms. Long.

Ms. LONG. Thank you, Mr. Chairman.

I would like to talk a little bit more about liquidity. Liquidity up to a point is good, but liquidity can be so great that it just increases the volatility in a market. We have been operating I think a bit under the assumption that, as long as we have dual trading, we can increase liquidity, and by increasing liquidity we have a more efficient market, a better running market.

I would like to ask you: Do you believe that in the past there has been at different points in time so much liquidity that it has led to greater volatility in the market, and as a consequence problems with tremendous price fluctuations?

Mr. **Melamed**. With all due respect, I know of no study from any academic source that would suggest that liquidity creates volatility. Just the opposite, in fact. Our experience and all academic studies have shown that in markets that have less liquidity, have more volatility. Price gaps develop between the current price and the next price simply because there are not enough bids and offers flowing to that marketplace.

All studies would underscore the fact that liquidity lessons volatility. The more liquidity you have, the thicker the market. The thicker the market, the less volatility. That is not to say that volatility cannot occur for a lot of other factors, and does, but not because of liquidity.

Ms. **Long**. But it can; once you get beyond sort of an optimal point, it can do that. And what I am asking you is: Have you seen that? And apparently from your response you have not seen that in your experience.

Mr. **Melamed**. I have not seen it, nor do I believe the theory is that it would occur beyond a certain point. As a matter of fact, all theory I have seen suggests the opposite. The more liquidity, the thicker the market, the less volatility.

Ms. **Long**. Up to a point, that is absolutely correct up to a point.

Mr. **Melamed**. I have not seen that point nor seen it in theory. I hate to differ with you, but from my reading and my understanding of what the market is, and from practical experience, there is no particular point. It is just simply the more liquid a market, the thicker it is.

As the gentleman who testified on behalf of the NCA, Mr. Josserand, said that as far as he is concerned, the more liquidity, the better. Sometimes the view is that there is something wrong with liquidity. Actually, what that means is more bids and offers and participants in the market.

Ms. **Long**. But it depends upon—the reason you have participation in the market depends upon whether you have speculation that is leading to liquidity, versus you have participation by people who have an actual end use for the commodity. And all of those variables are going to influence how positive liquidity is.

Mr. **Melamed**. The end-user of the market could not survive without the speculator because it is the speculator who takes the risk. The perfect market where there is no speculator, you can find in some places in the world, but they have no market. And you are acquainted with those places.

We need the speculator. The speculator's bids and offers are no different in the marketplace than is the end user's bid and offer. The bid and offer is the same. It is called liquidity.

Ms. **Long**. But, of course, we need the speculator but we need to have some kind of balance between speculation and end use of the commodity, and all of these things have to, in order for the market to be fairly stable, be at some level of balance.

I think that what we are looking for here, and I would assume what you are looking for there, is a means of operating the exchanges so that we are close to that balance most of the time.

I am trying to get from you—I think I am getting a pretty reasonable assessment of where you stand and what you believe—what is a reasonable level of liquidity, how much dual trading contributes to that liquidity so that we can then determine, and I individually can determine, under what circumstances dual trading is in fact useful for the exchanges.

In your assessment, the more liquidity, the better. Is that a fair assessment?

Mr. **Melamed**. That is correct.

Ms. **Long**. Thank you.

Mr. **Melamed**. I do not know other than that what to think because we have both theoretical and practical experience supporting this. As far as the balance between speculation and commercial activity, each market has a different balance. There is no particular rule on that either.

Some markets that I am acquainted with that are very, very successful have as high as a 95 percent factor of commercial activity and only a 5 percent factor of speculative activity. On the other hand, I know of markets that are also very, very successful that have a 70 percent factor of speculative activity and a 30 percent factor of commercial activity, and yet they too are successful. And everything in between those two extremes can find balance and successful markets.

There is no particular rule I know of that can tell us what the optimum balance ought to be. The marketplace is the only one that can determine that, and thank God that we have a system of free markets that allows the marketplace to seek that kind of level.

I will say this. If the correct level is not achieved by the market itself, that market will not exist and it will die, and many markets do. But as long as the marketplace succeeds, then by definition I think it has found a level of balance that allows the market to exist.

Mr. **English**. Mr. Harris.

Mr. **Harris**. Thank you, Mr. Chairman.

Excuse me, Mr. Chairman. I promoted him. You know, I do not think there is a person on the committee who does not want to see that the integrity of the market is maintained, and I know that is a concern of all of us as well as you. And I know I do not want to see anything done that would drive the business overseas.

So I guess what I am asking you on the question of dual trading, what recommendation would you make to us? I know that, for instance, the cattlemen recommended an outright ban. Of course, our bill is sort of a—it does not, it is not an outright ban. It has got some limitations on it. What would you recommend to do on that?

Mr. **Melamed**. Thank you, Congressman, for the opportunity to respond to this important question. And in doing so, I would like to also refer to the chairman's question about the original proposal by the special committee to ban dual trading in mature liquid markets.

That same committee was reconvened recently when the CME's internal committee proposed an alternative to the special committee's ban on dual trading in mature, liquid markets. The special committee unanimously approved the internal committee's recommendation and said that it was fully equivalent to their own recommendation.

In response to your question, the internal committee recognized, as did the special committee, that a delicate balance exists between the perception that dual trading might allow someone—and it is true—to violate the rules—front-running, and so forth, etc.—versus the liquidity dual trading provides.

How do you find that delicate balance? It is suggested that if we could find a way to catch enough of those culprits that would use dual trading to their own advantage and to the disadvantage of a public customer, and if we could do that enough of the time to give us the level of integrity that we seek, then we could preserve the positive aspects of dual trading which is its liquidity. That level is the 90 percent verifiability for the timing of trades through the computerized trade reconstruction system.

And if we can achieve 90 percent verifiability, it is felt that we will catch the wrongdoer enough of the time that we can afford to maintain the dual trading system. The special committee agreed that this approach was clearly adequate and as good as their own approach.

Those markets that cannot achieve the level of 90 percent verifiability will lose the right to dual trade.

Mr. HARRIS. Thank you. Thank you, Mr. Chairman.

Mr. ENGLISH. Mr. Staggers.

Mr. STAGGERS. Thank you, Mr. Chairman.

Following up on Mr. Harris' question, the flaw in that would seem to be that if we set a standard of 90 percent, then we are telling people as long as you only do 10 percent, you are OK.

Is there another way we can do that as opposed to the "any" and "all," language that is in the bill. And I think that is what Mr. Harris was getting at, I think we are looking for ways to get around the "any" and "all," but if we say as long as you work toward the 10 percent, I realize that setting the standards works both ways. That is my question, if we say it is OK for 10 percent, 90 percent is a laudable goal, especially in today's society. But if we do have the increase in technology, I mean, why not have a goal of 100 percent and leave it to the discretion of the CFTC, or whatever?

Mr. MELAMED. We are not saying that if we have 90 percent verifiability, the other 10 percent is OK. That clearly is not in our intent and it is not the way this would work.

The 90 percent verifiability would be accomplished by a system that can detect 90 percent of any untimed trades. The rest of the system, however, is geared to detect anything within that other 10 percent. These trades may be timed correctly. Our CTR system cannot, however, tell us this. All our rules and the package of reforms is very very comprehensive. And we feel that with all these rules together, our exchange will have a surveillance capability we feel is second to none. There is one element we have recently agreed to do, which I would like to explain if I could.

Mr. **English**. Sure.

Mr. **Melamed**. What we are suggesting is that every morning, the previous day's record of transactions be given to every member of our exchange within an hour of the next day's opening so that each of the 2,700 members of the exchange, most of whom are not dual traders, can act as policemen themselves. By examining the record of the previous day's trades, they will be able to detect whether any funny trades occurred in their own pit, and come forward with supporting evidence.

As a matter of fact, many of our sanctions today are self-generated, as you know, by the exchange's floor membership. This has never been done by any exchange, and it is only made possible because computerized trade reconstruction—CTR—allows us the luxury of quickly reconstructing the previous day's trades. We can give our members this important tool the next day as another self-policing tool for that additional 10 percent. Indeed, we have many many rules in place that will be more than enough to take care of the other 10 percent, which may be timed correctly.

We are suggesting so comprehensive a package that I believe this committee will be very pleased. I know our goals are the same. I have no doubt that everyone of us has the same goal—to have our markets the most efficient and with the highest integrity possible. I commend you all, and of course the chairman, for moving forward in that direction.

Mr. **Staggers**. Following up once again with what Mr. Harris said, I think I agree with you that our goals are similar, our search for putting together some language which can accomplish that.

My understanding is the system that you have now could do about 90 percent anyway. What I guess I am saying is if we write that into law, shouldn't we—I do not know what you mean by the 90 percent. Shouldn't we have some flexibility to allow somebody else to review this and to say, well, maybe next year, or 5 years from now, you can do better; 95 might be the standard which we want to achieve.

I agree that 100 percent of anything is very difficult to accomplish. And I see the point, but I am looking at it from a legislator's standpoint of how we put together something that is less than the "any" and "all," of the 100 percent. Now, I am searching.

Mr. **Melamed**. I am too. I agree with you that we should always try for better. Certainly 90 percent is the goal we have in front of us at this moment. But what we suggested is that we give the CFTC the authority to make the determination whether we have achieved the 90 percent.

We do not want to be the umpire involved, because that certainly would not be fair. We would like the umpire to be unbiased, one with the capability to make that determination, and that is the Commodity Futures Trading Commission.

Mr. **Staggers**. Thank you. Thank you, Mr. Chairman.

Mr. **English**. Thank you very much, Mr. Staggers.

Mr. Sarpalius.

Mr. **Sarpalius**. No questions.

Mr. **English**. Mr. Holloway.

Mr. **Holloway**. Thank you very much.

I know the testimony has been that undoubtedly the feeling out in America is that dual trading has problems. I would like, just for the record, for the two of you with both the Chicago Board and the Chicago Mercantile, exactly what do your exchanges mean to this country, to the city of Chicago? Knowing that we have been told over and over of the problems that we are going to have with the Japanese taking it over exactly in jobs and money, what do these two exchanges mean to our country, the city of Chicago?

Mr. **Melamed**. Thank you for the opportunity to respond.

To the city of Chicago and State of Illinois, Chicago's four exchanges are the central economic engine in that area of the Midwest.

[The supplemental statement submitted by Mr. Melamed follows:]

More than 33,000 jobs are provided by the exchanges, their members and the organizations that provide services to them. Over 110,000 total indirect jobs can be attributed to exchange economic activity. More than $11 million yearly in property taxes is paid on buildings that house the exchanges. Nearly $1 billion is spent annually on exchange-related goods and services in the Chicago area. Member firms have an average of $4 billion on deposit in Chicago banks on a typical day.

Mr. **Melamed**. But those are not as important as the fact that our markets are now so central to the financial fabric of this Nation. I would like to relate an anecdote. After the 1987 crash, I met with the heads of those financial firms in New York that are at the top of the financial structure in this country. One of those gentlemen said to me that before you testify in Congress to the Banking Committee on these issues, remember that your markets now are such a financial resource in this country, that we dare not do anything that would destroy or hurt them or drive them somewhere else, because they no longer are simply an out-of-the-way little marketplace. They are now central.

In fact, the Treasurer of the United States, Mr. Brady, called it one market; the securities market, the futures market, and the options market are now one market. Each one of them is such an important element in the overall financial landscape that we cannot exist without any one of them. And, of course, the rest of the world would love to get their hands on our markets.

Mr. **Holloway**. Thank you. I mean, I know that we have to be very careful. But I think we have to realize that if we make the wrong move, we very likely could let the Japanese take another one of the many industries they have taken away from us out of our country.

I think we, as a committee, I hope we proceed cautiously. I am not here to tell you that I totally understand the working of the Chicago Board of Trade or the Chicago Mercantile. And I hope to gain in knowledge as we go on to educate myself toward it. But I just hope that we, as a committee, are very very careful with what we do to our country as far as driving this abroad. Thank you.

Mr. **Melamed**. Thank you.

The **Chairman**. Mr. Chairman, if I might have a question of Mr. Melamed, if you would.

I think you gave a very good, succinct, factual description of dual trading. My perception is that the dual trader is not the problem, but rather if you front run. Then the question I would like for you to address is if the front run may or may not be to the disadvantage of a customer. What is the experience in that area? Just detecting that someone bought for himself rather than for a customer, gives us numbers in a vacuum. You and most of the witnesses here are the experts. We deal mostly from theory rather than from actual experience. We have to accept that and appreciate that. But I would hope that we can put in the record a little more explanation in the whys and wherefores and you address it in part.

Could you help us with that, Mr. Melamed?

Mr. MELAMED. I would be pleased to, Mr. Chairman.

I want to say, first off, that our rules very explicitly label any front running as a violation. Front running simply means that when a broker has an order for a customer in hand, he dare not do a trade for his own account ahead of that order for the customer.

That does not mean that when he violates that rule he automatically injures the customer. That has to be examined in a courtroom or before a committee. Let's say the broker filled the order for the customer and for himself at the same price and everybody got the same price. Of course there was no injury involved. But the rule had been violated just the same.

We look at that very, very strictly. In effect, you cannot and dare not violate the rule of front running. We feel that dual trading does give the opportunity for that kind of thing. That is why we are here and talking about it.

But I must tell you, Mr. William T. Cherry, staff director, of this subcommittee correctly stated to this committee that dual trading is not inherently evil, that banning dual trading does not cure all evil, and that there is nothing that cannot be done without dual trading that can be done with dual trading.

In fact, he indicated that there are only two kinds of violations that can occur because of dual trading: When a broker trades ahead of a customer's order; and taking a position against a customer. This kind of thing is one of the easiest abuses to detect. If you ban it, all you are going to do is allow that dual trader to find a different way to violate. That violation is going to occur if he chooses to violate. And we have to find him anyway.

So you are right in saying that to ban dual trading will not cure the evil involved.

The CHAIRMAN. The next item, Mr. Melamed, you mentioned briefly the problems with the securities industry in New York. And you mentioned your resources as to information.

Could you expand on that? I know that we heard that you were supplying to the SEC information that they did not have readily at hand.

Mr. MELAMED. I could do it best by telling you this incident.

Mr. Nicholas Brady, who is now Secretary of Treasury, headed the Presidential task force investigating The 1987 stock market crash. When he visited our exchange within 1 week or so after the crash, he sat down with us and had a long list of the kind of information that the committee he was heading would need in its study. He asked us how long it would be before we could give him our response to this information, a lot of statistical information about the trades that occurred during the week of October 19. We told him that we have that information, and can give it to you before you leave today.

He was astounded because the securities world was unable to give it to him for weeks thereafter, months in some cases. Yet our Computerized Trade Reconstruction—CTR—system was such that we were able to give it to him within days after the occurrence.

In fact, as I suggested today, we are ready with a reconstructed trade register the day after. No other exchange I know of has that capability in today's world; in the United States certainly.

The CHAIRMAN. Would you also mention briefly your computerized process, your GLOMEX operation?

Mr. MELAMED. I would. What we recognized, Mr. Chairman, was that the competition that we face with the Japanese and the Europeans transcends our working day. Because, you know, the world has now shrunk to a point that these competitive markets are everywhere. People do not wait until our markets open the next morning to trade, to do their hedging, to do whatever they need.

In fact, it used to be we were all protected with a geographical blanket that protected our markets from competition. It is no longer true. So we decided that we must lead our industry to create an "after-hours" system. And the best system to create, we thought, was electronic because that would work best for all 24 hours, the 16 hours that we are not physically open.

We went to the largest communications organization in the world, Reuters, and with them created GLOBEX, an "after-hours" transaction system that will be launched sometime later this year or early next year. For the first time in history, we are leading the financial service world to a 24-hour transaction system. And I must say, everyone has followed our lead, including the securities world.

I notice the over-the-counter industry has moved in the same direction. The security options industry has moved in the same direction. But it was our exchange that led the way. And recently, as you know, the Chicago Board of Trade which created their own system of a similar nature and the Chicago Mercantile Exchange have entered discussions to unify those two systems so that together we could present to the world a cost-efficient system.

The CHAIRMAN. Thank you very much, Mr. Melamed, and let me apologize. I called your GLOBEX, GLOMEX. I have been working on the Mexican foreign debt. And everything has been "mex" for the last couple of weeks.

Mr. MELAMED. I did not even notice that.

Mr. ENGLISH. Thank you, Mr. Chairman.

Mr. Morrison.

Mr. MORRISON. Thank you.

The capabilities of GLOBEX are exciting.

Is there a potential that it sets the stage for the incursion of fully computerized trading on into your normal trading day?

Mr. MELAMED. I do not believe that that is likely in the foreseeable future.

We have yet to prove to what extent liquidity can be generated on a computer. We do not know that. We are experimenting. Now, if you ask me what will it look like 20 years from now, I do not know. But in the foreseeable future, I do not think so. I believe that the electronic system GLOBEX and AURORA, that we hope to launch in the near future, will succeed because it will depend on and key off the liquidity of open outcry that is created in the open outcry fashion during our trading day.

That liquidity will work as the engine to succeed with the electronic market later.

Mr. MORRISON. But it will demonstrate a technology that if and when the institution is ready to move in that direction, it could be utilized as even a replacement for the current human involvement in the pits.

Mr. MELAMED. Theoretically. That is speculative, but theoretically you are, of course, correct. I merely say that I cannot foresee that in a foreseeable timeframe.

Mr. MORRISON. It would be interesting to see how the institution responds. I think your approach to it is a superb combination.

I wanted to ask about something that I do not believe anyone has talked about and that is off floor trading. It is not included in our chairman's bill, and yet without knowing exactly what all was involved in the FBI investigation, maybe a part of what they find that reflects some problems out there.

Could you just give us an overview of your concerns with or how off floor trading could be controlled, regulated, restricted?

Mr. MELAMED. Well, we clearly do not know what the investigation will show. You are correct.

As a matter of fact, our best advice is that not much of the investigation will in fact indicate a lot to do with dual trading. I mean, there are violations involving taxes and there are other kinds of customer cheating that do not have anything to do with dual trading. And there might be some off exchange things that we do not know about, you are right.

Off exchange has always been a problem for the exchanges because we have no authority. In fact, some years back we went to Congress, and together, as you may recall, worked out the creation of the National Futures Association. The NFA is the authority over off-exchange matters, ordained by the CFTC to help the CFTC in such areas as financial monitoring of off-exchange entities, that is entities that are not members of exchange.

And so it is an area that we have some concern with, but we have no authority over. The National Futures Association does an extremely good job in monitoring some of that area. And the CFTC has to do the rest.

Mr. MORRISON. You are comfortable then that NFA and their working relationship with the CFTC adequately covers that area?

Mr. MELAMED. I must in all honesty advise you that I am biased, since I am chairman of the NFA. Yes, I am comfortable and I believe the NFA does an excellent job, but it is very self-serving for me to say so.

Mr. MORRISON. We love confidence around here. It is a product that is all too often in excess supply.

The Commodity Futures Trading Commission yesterday sort of got beat up and I would like to, even though my time is up, just ask one more simple question.

Your general observation working relationships between the exchanges as being essentially self-regulating and the CFTC. And as we go through this process, do the dynamics need to be changed?

Does the level of authority need to be changed? More of an editorial type question, I guess, than a specific one.

Mr. **Melamed**. In our workings with the CFTC, although many of our members enjoy when a Federal agency gets beat up and applaud when that happens, I must say that we, as leaders of the exchange, have found the CFTC to be an exemplary agency. It is run extremely well and does a very very efficient job.

As a matter of fact, we have a direct comparison that many of our members do not because we deal with many Federal agencies, not just the CFTC. And in almost every instance, I would say that the CFTC comes out with higher marks than do other comparable Federal agencies. Our experience has been just the opposite. We find the CFTC to be very professional.

As a matter of fact, we are, as you know, strongly in favor of permanent reauthorization for the CFTC. I believe the bill that the chairman introduced also includes that provision, which we support.

Mr. **Morrison**. Thank you very much.

Thank you, Mr. Chairman.

Mr. **English**. Mr. Grandy.

Mr. **Grandy**. No questions.

Mr. **English**. Leo, I have some additional questions and I think probably some of the other members will too.

I want to ask you to put on the hat that you were wearing on April 19 when you signed the report. With regard to the provisions dealing with dual trading, I noticed in there that it bans dual trading in all contract months that reach the level of mature liquidity.

I suppose the question comes in, and this would be determined by the board of governors and based on market conditions and so on. What is the definition by yourself of mature liquidity?

Mr. **Melamed**. Well, we use those words because there is no objective way in which to measure a mature liquid contract. We used them and indicated that it was up to the CME's board of governors. This special committee, in its report, stated that the only way it could make that judgment and feel comfortable about it is if they allowed the market experts to make a determination on a case-by-case basis which market is sufficiently mature and liquid to withstand the hit it might get by losing some dual trading liquidity.

The special committee used the words mature liquidity with the understanding that you could not say categorically which number is right and which number is wrong. And they allowed the board to make a determination market by market, in fact, contract month by contract month. That was their idea and that is how they proceeded.

Mr. **English**. And that basically is the provisions under the bill. The bill sets a certain number. It provides and allows for the exchanges to come before the CFTC. The CFTC instead of the board of governors then would be the one that would make that determination. So they are very similar in that manner as far as where the determination would ultimately end up, the CFTC on one hand, the board of governors of the exchange on the other.

Mr. **Melamed**. We have no quarrel with the goal, as we have talked before, of your bill. Our difference is simply that we do not believe that an absolute number is the way to approach this, because we fear that and we do not feel that it is going to work in a practical way, that the CFTC will act in a timely manner.

It might very well be, with all due respect to the CFTC, that they will not act in a timely manner, because the system does not work that way. By the time the illiquidity that has developed around a given market has hurt that market, it is too late to change the requirement. If we lower the requirement from 7,000 to 1,000 and the market is already hurt by it, you cannot bring a market back quickly.

And so, as in many things that are very sensitive, we feel you cannot wade through a process that is, by its own nature, bureaucratic and will not work as kindly as is necessary. We do not want to take that chance.

Mr. **English**. But the point that we come down to though on the issue of liquidity in discussing it with some of your members as well as members from the other exchanges, it is my understanding within the industry generally perceived when a contract hits the level of 5,000 a day, it is generally considered to be mature liquid contracts. Is that not true?

Mr. **Melamed**. I do not know that—I mean, these are opinions other than mine, but I do not know that there is such a number that we could say. I know that some small markets are adequately liquid at 5,000 and some are not; some are not liquid at 20,000. It is a question of whether the order flow is constant or at least is consistent every day or every month during the course of the year.

Mr. **English**. But the basic issue that we are talking about here though comes down to the question as to whether it would be, as the proposal was originally intended, whether it would be the board of governors of the exchange or whether it would be up to the CFTC to determine whether a particular contract is a mature liquid contract or not. Is that not true?

Mr. **Melamed**. You will note that when our internal committee suggested a 90 percent verifiability threshold instead of mature liquid, the special committee to which you are referring, unanimously accepted that as an adequate alternative to its own proposal. They recognized that there is so delicate a balance between trying to correct the perceived wrong and the loss of liquidity that one cannot be so absolute. They felt that the 90 percent verifiability approach was as good and perhaps better.

Mr. **English**. It is my understanding though that the recommendation that you and the special committee made to the membership met with a very strong rejection, opposition by the membership to those particular proposals. And that these were drafted in place of those as a response to that strong opposition. Is that not true?

Mr. **Melamed**. There were vocal objections, of course. There was a segment that does not want any restriction on dual trading, of course. But I do not know that was the vast majority.

The internal committee that wrote the substitute alternative and presented it to the special committee, was composed of people that clearly understood the problem. And no one pressured the special committee to agree that what the internal committee suggested was in every way as good as their own proposal.

I do not believe it was in response to any major objections from our floor. There were some that objected, of course. There are objectors in every society or social structure. But that was not a pressure that our internal committee bowed to.

Mr. ENGLISH. Mr. Coleman.

Mr. COLEMAN. It has happened not just today but yesterday also that we continually forget about the exemptions, exclusions, opportunities for flexibility both written in the bill and in your proposal.

We talk in stark contrast. We are either for dual trading or we are against dual trading. Dual trading is going to dry up the markets or it is not going to drive things off-shore. We cannot talk in terms of black and white, because your own proposal prohibits dual trading. If I wanted to stop at that, it would be a rather unfair characterization.

I think it is very unfair for people to suggest that the bill prohibits dual trading and stop at that, because we provide opportunities to exempt exchanges from the prohibition, and you have addressed those in your written testimony.

At the same time you prohibit dual trading if a market does not come up with a 90 percent standard.

Mr. MARTINEZ. That's right.

Mr. COLEMAN. So let's all be a little more forthcoming in how we discuss these issues. What is it that we do not have in our bill other than "any and all" and the 100 percent verifiability—which is your interpretation, and we understand that? Is it that we do not provide enough flexibility to the Commission to deal with certain problems? Your own proposal provides for the same exemptions, written authorization of the dual trade, for example. We have the spread issue. We have tried to address that. Do you have that?

What is it that is different about the two proposals other than that we have a standard which is higher—but which could be modified. We are open to suggestions and modifications of some sort.

Is there really any substantial difference, Leo, in what we are saying? Other than the degree, I guess, you are at 90, you may think we are at 100.

Mr. MELAMED. Well, other than the degree, of course. The approach is different because ours is based on a 90 percent verifiability of timing of trades, and the proposal of the bill is based on a volume statistic. The volume statistic in itself is an arbitrary number.

Mr. COLEMAN. As a threshold, but also it can be amended by the Commission itself. They could set it at 300,000 contracts, and everybody would be——

Mr. MELAMED. I doubt if they would because that is the point. The Commission is not going to change the will of the Congress, nor should it easily. You would not want that and I would not want that. It would be a difficult process for the Commission to ignore the suggested requirement of Congress. It always is a difficult proposition.

So in the kind of give and take that happens after such a bill that has a number in it becomes law, it becomes almost near impossible to change the number. By the time the number is changed, a given market has suffered and it will be too late to save.

Mr. **Coleman**. In all due respect, if we were to take your language and draft it into legislation, the 90 percent would be put into law, and you would have the same impact, if a contract could not reach that. True?

Mr. **Melamed**. Yes, but it is not based on a volume statistic. It's based on a statistic of verifiability of all the trades that occur.

There's one more element that our attorney would like to mention. If I could ask him to with respect to the bill that I have not touched on.

Mr. **Salzman**. If I could, I hope this isn't too technical, but some of the exemptions are slightly troublesome, especially the one on brokers who make errors. The bill seems to say that a broker who makes an error must wait until the next morning's opening to trade out of his error. The people we've talked to at the exchange have said that it will make it utterly impossible to act as a broker because the range of costs that could be involved in that are just so enormous.

Everybody at our exchange, at least—everybody I've ever talked to—agrees that a broker must be free to trade out of his error immediately, otherwise the cost of brokerage, which is now between $.75 and $1.50 or $1.75 either has to go to an infinite level or these people will not act as brokers. There is just not enough money in it to take those kinds of risks. They are taking $100,000 risks for $20.

Mr. **Coleman**. These are types of things which obviously can be addressed and modified, and we respect and want and seek your expertise along these lines. So I think we are getting into some, as you say, if not technical, at least some side-stream issues, and I want to pursue a couple of the mainstream issues here, if I might.

This suggestion that we are going to force things offshore is a real easy one. We heard that in 1986, in all due respect, in the last reauthorization. It has not necessarily occurred.

The analogies to the securities markets, if we did not have an insider trading violation of law, there would be some who would say, "If we have such a law against insider trading, we might be driving all the securities offshore." I do not think anybody wants to eliminate that segment of securities law because somehow Tokyo or Taiwan or somebody might open up a market and allow insider trading.

We need to have the safegaurds here, not just because we are afraid of competition, that somebody else will have less safeguards, as long as we do not destroy our markets. So all this driving offshore business is an easy argument which is difficult to suggest that the answer is going to be more suspicion of our markets, less things nailed down, more perception problems that somehow this is going to attract business.

Mr. **Melamed**. May I respond to the issue of offshore competition?

Mr. **Coleman**. Sure.

Mr. **Melamed**. That is not simply an imagined issue. I agree with you that we want to have markets with integrity. Clearly, you are right about that, but unmistakably the issue of offshore competition is very serious.

From 100 percent of futures market share, in the last several years, we have gone to 65 percent. If the auto industry or the microchip industry are examples of what the Japanese can do to our market share, those are serious competitive factors that we as Americans must understand and be very careful with. While I do agree with you entirely that our markets must maintain integrity, we cannot afford to ignore the competitive issues that foreign markets do represent.

Mr. **Coleman**. Have you seen any pull away in our T-bill markets by the Japanese?

Mr. **Melamed**. Which market?

Mr. **Coleman**. Treasury or other credit markets?

Mr. **Melamed**. Absolutely.

Mr. **Coleman**. Would some of that be as a result of what, what reason?

Mr. **Melamed**. The Japanese created markets that attract the business we invented and are taking that business from us. That's true in U.S. bonds, in Eurodollars, and they are now attempting to do so in currencies.

Mr. **Coleman**. But it has not been because of anything that we have slapped on from this committee or the high confidence that you have voiced in the Commission, has it?

Mr. **Melamed**. On the contrary. Your committee has thus far been very supportive and in full understanding of the value of this industry. What we are simply afraid of is a change in direction.

Mr. **Coleman**. Let me ask one or two other questions, if I might. The issue of front running, Leo, has been brought up. Front running today is a violation of law because it is fraud. Is that not the case?

Mr. **Melamed**. That's right.

Mr. **Coleman**. So there should not be any question that it is already a violation or a wrong that is being looked for by the exchanges and by the Commission.

Mr. **Melamed**. That's correct.

Mr. **Coleman**. One final question about dual trading in the audit trail. With GLOBEX going to a computerized trading system, you have in fact constructed something that would change the terms of our bill. Correct?

Mr. **Melamed**. On the contrary——

Mr. **Coleman**. Is 100 percent verifiable?

Mr. **Melamed**. Yes, but in one respect, Mr. Coleman. It isn't possible to live within the bill because on the computer there should be no ban on the dual trader at all.

Mr. **Coleman**. That is correct because he would be found out.

Mr. **Melamed**. Yes, it's 100 percent verifiable.

Mr. **Coleman**. That is what we are saying.

Mr. **Melamed**. Exactly, so that your bill would not fit the computer world at all because we shouldn't have any 7,000 or any requirement.

Mr. **Coleman**. You would have met the exemptions, and the dual trading would occur as you directly state. The problem with the dual trader is if you traded ahead, he would be found out because you had a system set up already.

Mr. **Melamed**. My suggestion only is this: In your bill you might want to adjust the language that shows the difference between a computer-generated environment and a floor open outcry environment, if I might suggest that——

Mr. COLEMAN. That is indeed the question, isn't it, open outcry? Let me ask you a completely different question. We had some testimony yesterday about basically the Chinese wall. In the construction of the Chinese wall with a large broker like Merrill Lynch trading for its own account and trading for customers, could you tell us a little about how you look at that Chinese wall? You at the exchange have the power to audit those now, correct?

Mr. MELAMED. Yes.

Mr. COLEMAN. And any problems—have you seen any problems with the breakdown of that Chinese wall, and would you explain what that is for the record?

Mr. MELAMED. Could I ask our attorney to try this one?

Mr. COLEMAN. Yes.

Mr. SALZMAN. We absolutely understand the problem, and we have now created a surveillance tool, a computerized surveillance tool to deal with it. We search the market for large price movements in short periods of time, and then look for all orders entered just before and after those moves, then we can trace those orders back upstairs as well as the floor.

So given that tool, which our compliance people have now created and which will be put into effect very shortly, we believe will be competent to deal with upstairs abuses as well as floor abuses of dual trading or trading ahead of customers. It's a pretty smart idea, I think, and it works because we have the CTR system operating at this point.

Mr. COLEMAN. And the CFTC has not found any problems in reviewing your audit.

Mr. SALZMAN. The CFTC finds problems every time they review us. It's part of their job. They give us a list of 8 or 10 corrections every other year, and they come back 1 year later to make sure we have implemented them. We know that no matter what we do, they are going to find 8 or 10 things we have to correct the next year, and we expect it. It all helps build Leo's confidence.

Mr. MELAMED. That's correct.

Mr. ENGLISH. Mr. Tallon.

Mr. TALLON. Mr. Chairman, thank you. Anybody that wanted to use a broker that was not a dual trader they could certainly have an opportunity to use a broker that was not a dual trader or used the Globex system which is a fully automated system. Is that not true?

Mr. MELAMED. That's true. In the present world, any customer can direct his orders to a nondual trader if that's what he chooses.

Mr. TALLON. Ms. Long was asking some very good questions about stability and liquidity and its impact and effect on stability, and I think your very good answer was that liquidity created stability in the markets. In the legislation that we have before us in trying to define or determine a mature liquid contract with the 7,000 volume traded daily, would it be better in trying to define a mature liquid contract if that was a course that this committee is going to go to—think about the bid-ask spread on any contract traded on any exchange?

Mr. **Melamed**. There is no shorthand rule I know of for determining mature liquid. That's a hands-on kind of approach, feeling the market, seeing the kind of bids and offers the market gets on a daily basis over weeks and months by the people on the floor and in the business and in the commercial area of activity.

I don't know of any rules that can tell you bid-ask or otherwise.

Mr. **Tallon**. And again, I was not thinking about any strict rules, but we have not really—for exemptions that Mr. Coleman talks about in the bill—we have not talked about the CFTC and liquidity period, but if we are talking about liquidity somehow I think we have to look at the bid-ask spread rather than an arbitrary 7,000 contracts traded daily.

Mr. **Melamed**. Well, you're clearly right that the bid-ask spread is an indicator of liquidity. A spread that is consistently small between the bid and offer is indicative of a much more liquid market than is one that has a very big spread between the bid and offer. That was part of the answer that I gave Ms. Long in terms of price gaps.

A large spread between the bid and offer will create large gaps of trade between a price and the next price, and is indicative of a less liquid market.

Mr. **Tallon**. And a less mature liquid contract.

Mr. **Melamed**. Exactly.

Mr. **Tallon**. So, certainly that might be a way to determine liquidity in a contract on any exchange, in my mind, if that had to be done by the CFTC to form what exemptions would be applicable.

Bill, how many traders on the Mercantile Exchange has the Justice Department ever prosecuted specifically for trading ahead of a customer?

Mr. **Brodsky**. None to my knowledge, Mr. Tallon.

Mr. **Tallon**. Bill, if criminal penalties, mandated criminal penalties were written into this legislation for traders that were trading ahead, what kind of impact do you think it would have on people that are involved with dual trading? Would you want to comment on that because that is certainly something that I have an interest in and we have discussed?

Mr. **Brodsky**. Our view generally is that there is certain conduct right now that is violative not only of our rules but of Federal law, and I don't think that there is any need to do anything further. My counsel might be able to add to that, but I believe that our own enforcement program plus the oversight of the CFTC has had a very important prophylactic effect over the last several years to deter this type of conduct.

Mr. **Salzman**. I can only say that I saw the Justice Department's reaction to the proposal. I know they are very nervous for fear that somebody will interpret the change in law as if the previous boss said there was no penalty. We have been cooperating as fully as we can with the Justice Department, and we don't want to support anything that they are against in this matter. I think we have to leave it at that even though we understand what you're trying to do and why it's important.

Mr. **Tallon**. And yet, the Justice Department has never brought criminal charges against anybody for trading ahead of a customer, and certainly if I were a dual trader, which I think can be very beneficial that to provide liquidity and efficiency to these markets, I do not think that I am going to think about the—I am not going to give much thought at all to the illegal practice of front running if that is a part of this legislation. That would be my view anyway. I do not know I would want to deal with trade anymore.

Thank you.

Mr. ENGLISH. Ms. Long.

Ms. LONG. Thank you, Mr. Chairman. I would just simply like to make the statement that right before a market crash you have a high level of liquidity usually due to a high degree of speculation, and what we really need to find in this legislation, what we are willing to do in this legislation is work toward regulations that keep liquidity at a healthy level and speculation at a healthy level.

Thank you.

Mr. ENGLISH. Mr. Grandy.

Mr. GRANDY. Thank you, Mr. Chairman. I apologize to the committee for being tardy this morning.

Mr. Melamed, I wanted to ask you your opinion of something. I have looked at your testimony briefly and hoped to have some time to ask you about some of the things in it. But a couple of days ago, Chairman Gramm was before us, and I asked her a question that related to insider trading, and I asked her for her definition of it as it relates to the commodity exchanges. The definition, at least to this member, was not intelligible.

Can you tell me what insider trading is in your exchange and how do you police it?

Mr. MELAMED. Well, insider trading in the classic sense has to do with, say, knowledge of a corporate report by someone within a corporation knowing the dividend report or how the company is doing or some special product that might be coming out. Those are the classic cases of insider trading.

None of those exist in futures market because the product that is being traded is not corporate-owned. The product that is being traded is everybody's product. Everybody knows the specifications of the product. These specifications don't change. Everybody knows what it is that is being traded.

The only kind of insider trading that occurs in terms of futures markets that come to mind is, for instance, the broker who has an order in his hand from a customer. The broker knows what that order is, and then deals for his own account because he understood what that order from his customer might be. He has some special information that nobody else has. We are very mindful of, and very concerned about that kind of thing.

But the other kind of insider trading that might occur is if there is a Federal report about a market, such as a market report on the trade gap or something from the Labor Department on employment figures, or a cattle report that might be coming out. A Government employee might have that information beforehand, and use that information to his own advantage, sometimes in conjunction, say, with a broker. That would be the same kind of inside information you are talking about.

Mr. GRANDY. And how do you prevent that?

Mr. MELAMED. We prevent that, first of all, by having a strong surveillance force that is cognizant of this kind of thing, especially the first example I used of the trading ahead of the customer order. We obviously have the ability to look at a broker's own personal account to determine every trade he ever made in a given day, and compare it to when he received orders from a customer, and whether they were close in line or not.

Mr. **Grandy**. Well, let me ask you this. Several years ago, our colleague Neal Smith introduced a bill, which never became law, to prevent insider trading, and it reads as follows, and I would just like you to comment on whether or not insider trading could be banned statutorily.

Basically he is amending the Commodity Exchange Act to say:

> As used in this subsection, "insider" means any individual who has access to material information not generally available to the public about present or anticipated cash or futures trading or present or anticipated cash or futures positions for which such individual is not a party in any commodity of any other persons where such trading or positions are in amounts at or above Commission designated reporting levels as specified pursuant to section 4(i) of this act.
>
> No insider shall own, control, have a beneficial interest in or enter into any contract or contract for future delivery in any such commodity on any contract market.

What is the problem with that language?

Mr. **Melamed**. Well, the problem with that language is that it doesn't attack the examples I gave you. What Representative Smith has a problem with is that, for example, a grain company knows it will be selling grain to a foreign body and puts on positions to protect itself with respect to those sales. Under the bill, the grain company would not be allowed to hedge and protect itself.

This is true in cattle or in hogs or in other commodities. These major commercials are using the special inside information they have because they have done the sale, and our markets are exactly for them to use under those very circumstances. They ought to be hedging their forward needs in our market, and using that information to their own advantage, because the advantage for them is that they can continue to make these sales.

The bill would prevent, in fact, the function that is very important of our market.

[The supplemental statement submitted by Mr. Melamed follows:]

> The bill would interfere with the effective operation of futures markets to the overall harm of farmers and commercial market users. It would discourage every professional market user from seeking the information necessary to allow the market to fairly discover the appropriate price.
>
> Considerable information about supply and demand in the marketplace is discovered by the legitimate observation of buyers and sellers. The Smith bill would destroy any incentive to acquire this information, to the extreme detriment of the market.

Mr. **Grandy**. I understand that, I believe, to a point, but do I hear you say that this amendment, this bill that Mr. Smith introduced, I think, 6 years ago, would basically outlaw hedging for large companies?

Mr. **Melamed**. That's right.

Mr. **Grandy**. What about the small investor, what about the small trader who would not have access to this information? Does this prohibit him or does this in any sense give him a more even position with his larger counterparts?

Mr. MELAMED. The theory of markets—and we live within that theory—is that the price structure of the market, the movement itself, is indicative of what's going on in the market. Large commercial buying obviously, or selling, puts a market up or down, and the small investor has to have some understanding why it is going up.

The information generally is available. It is very seldom that you don't know after a period of 1 or 2 days who has been buying and who has been selling as to why the market went up, and then you can make certain assumptions as to why that commercial activity went on, and usually those assumptions are correct.

So that I think the small investor is generally not so at the mercy of not having the information because he has the information of price movement.

Mr. GRANDY. I see my time has expired, so I will not belabor this. I understand the small investor has the information on price movement, but usually after it is too late, and I, of course, am referring to some of the problems that happened in the bean market last week which had a very significant impact out in my area.

Mr. Chairman, thank you.

Mr. ENGLISH. Mr. Nagle.

Mr. NAGLE. The proposals with regard to the disciplinary committee seems to have drawn the ire and hostility of most of the exchanges, but we have not really spent a lot of time talking about it in here.

Could you elaborate a little bit on what your specific objections are to the committee draft with regard to the disciplinary committee composition?

Mr. MELAMED. Our special committee, of which I was a member and Mr. Brodsky was a member, made the original suggestion that there should be an outside member with voting privileges on the major exchange disciplinary committees which will address the perception of clubbiness and closed room kind of decisionmaking. We want to open up the process and show the world that indeed we are not afraid of an outsider being present.

We have no objection with your recommendation in terms of the committee structure.

Mr. SALZMAN. The only real problem—maybe it is a lack of understanding on our part—is the suggestion in the bill that the committee not have a majority of people on it who are in the same class of trader or same class of person as the person being tried. Nobody at the Merc really understood why that was necessary, and we found that it would be counterproductive.

Our clearing house committee, which disciplines clearing members, is made up of other clearing members because they are the ones who understand the clearing operation. There has never really been a sense that we were aware of that anybody felt that that was unfair or operated badly. Moreover, our committee that punishes floor traders for trading abuses is made up of other floor traders, and generally they are the ones most eager to punish the offending floor trader. There hasn't been any complaint about that.

Mr. MELAMED. I didn't know you were referring to the composition in terms of peers. The peers are the ones that know the most about the rights and wrongs of a situation, and are best able to make the judgment.

Mr. NAGLE. Let me yield to the chairman.

Mr. ENGLISH. I will be happy to clarify that since there seems to be some question about it.

The point that was made, and we did through the course of our inquiry, complaints were made to me and to members of the staff that basically it does become difficult for floor traders and brokers is if you are sitting there in the morning and you have to vote against the guy and vote a stiff penalty on him and then turn around in the afternoon and go out to do business with him.

That was the reason for the particular provision. The provision is that you could go outside the exchange if you wished, but it should be someone that does not have to directly do business with that person day in and day out that should make the judgment. It also says the majority, it does not say all, and that is the reason for it.

Mr. NAGLE. Mr. Chairman, let me reclaim my time, let me ask you a question maybe it is as much to the Chair as to the witness. When we are borrowing or when we are restructuring these disciplinary committees, are we doing it on the basis that one pit will not be—we are assuming that everybody on the committee is from the same pit or are they from different pits?

Mr. MELAMED. They are from different pits, and that's a very good point. I was going to respond in that fashion. Our committees are, in fact, comprised of members from different trading pits. In fact, we have a very healthy mix. If you are dealing with a violation that, for example, occurred in cattle, it's very likely that the majority of those members will not be cattle members. We try to structure the committee differently so that you avoid the very situation the chairman correctly indicates is difficult.

Mr. NAGLE. Are the disciplinary hearings open to the public?

Mr. MELAMED. The results of these hearings are public. We are suggesting that one nonmember be on each of those disciplinary committees. That would create an additional element of some outsider presence.

Mr. NAGLE. Would there be a problem if they were open to the public?

Mr. MELAMED. There is a problem in terms of the legal necessities involved with the internal mechanisms of the exchange. I don't think that there has ever been that kind of objection about the proceedings of our exchange. There has been objection that there aren't outside members, and we are trying to correct that.

Mr. NAGLE. What percentage of—what number of disciplinary actions did your committee take last year? Did the various disciplinary committees of your exchange take?

Mr. MELAMED. I think the number is in the testimony, and I'm going to try to find it. While it is being searched for, I will say that it is probably a record we are very proud of in terms of how many cases we instigated, and how many people we penalized.

There were a total of 217 penalties, 313 fines in 1986.

Mr. NAGLE. Wait a minute, 217 penalties and 313 fines? What's the difference?

Mr. MELAMED. Excuse me, the figure in 1986 was 33 participants penalized, in 1987, it was 69, in 1988 it was up 105. The fines were

$313,000 in 1986, $1,715,000 in 1987, $811,000 in 1988. In 1986, there were no expulsions, in 1987, there were eight expulsions and in 1988, there were two expulsions. In 1986, there were suspensions of 238 business days, in 1987, there were 12,392 business day suspensions, and in 1988, 6,110 business days suspension.

Mr. **Nagle**. Two questions. It looks to me that the traders are getting more dishonest as we go or we are getting better at detecting them. We have gone from 43 to 69——

Mr. **Melamed**. Better detection.

Mr. **Nagle**. What is the nature of the abuses they are being fined for, suspended?

Mr. **Melamed**. Well, a lot of them have to do with violations that occur by virtue of getting ahead of the customer trade.

Mr. **Nagle**. Abusing the dual trading process?

Mr. **Melamed**. Abusing that. They have to do with doing something that takes away from a customer the rightful trade, not necessarily getting ahead, but simply taking advantage in another way not giving the customer the rightful trade that he ought to receive.

I am being given a following breakdown of our trades of the violations from the year 1986. It is in table 2 of the appendix to 1988, and here are the following breakdowns, if I could.

Sixty-two were prearranged trading infractions; 15 were trading opposite of customer infractions; 6 were a combination tradings; 14 were outside the exchange hour of pit trading; 3 were disclosing orders; 6 were withholding orders; 1 was trading ahead of a customer; and 5 were fictitious, what we would qualify fictitious trade.

Those are your statistics from your committee.

Mr. **Nagle**. No. The curious thing is that we have 4,369 and 105. How many of those people are still trading on the exchange, all of them, except 10?

Mr. **Melamed**. Well, those that were not expelled and are still not under suspension, I don't know the exact statistics. But once the suspension is over, and if they are not expelled, of course they could go back to the floor.

Mr. **Nagle**. Is there a system on your exchange for—if I run a stop sign once, it's a $10 fine; if I run it twice, it's a $20 fine; if I run it the third time, you take away my privileges? Is it graduated here and time competitive?

Mr. **Melamed**. Absolutely. Absolutely. And the fines are very, very heavy, Congressman Nagle.

As you probably know, our exchange penalties were at the $250,000 limit before the recent structures recommended for everybody. So we have been at a very, very high level, and in fact have generated the largest bonds in the industry.

Mr. **Nagle**. Going back to bring this full circle, with the indulgence of my chairman, you are suggesting—in your statement here I thought you were a lot stronger about the committee's recommendations than, I guess, your initial testimony.

You say we strongly oppose the imposition of composition requirements on exchange of disciplinary committees. It would be rash of Congress to mandate changes in the absence of a documented failure of the current disciplinary committee system.

You are saying, however, you are willing to accept the requirement that, perhaps from us, that there be outside members on the disciplinary committee?

Mr. MELAMED. That's right. We recommended that ourselves.

Mr. NAGLE. Is the problem with the elimination of the peer process the lack of knowledge that would take place on the various disciplinary committees?

Mr. MELAMED. Again, the peer pressure?

Mr. NAGLE. The peer knowledge. I mean if you're working in a certain area, I mean if you're being judged by your peers, your peers are more likely to quickly know that that in fact is a violation or an abuse?

Mr. MELAMED. That's correct.

Mr. NAGLE. Well, I thank the Chair for his indulgence.

Mr. ENGLISH. Mr. Gunderson.

Mr. GUNDERSON. Thank you, Mr. Chairman.

Is it fair to say, having read your testimony, Mr. Melamed, that you would favor just a simple straight reauthorization of present law only making it permanent?

Mr. MELAMED. Well, we recommended many changes that we will offer to the CFTC.

As far as reauthorization goes, we favor reauthorization.

Mr. GUNDERSON. I get the impression that you don't want anything else in the statute, that what you really want us to do is simply reauthorize present law and let any decisions that are made be done by CFTC.

Mr. MELAMED. Well, I don't know how that necessarily has to work because we have made recommendations. I don't want to suggest how that should happen. We expect our recommendations will become law in one form or another, whether they take the form in legislative action by you with an order to the CFTC, or whether they take the form of CFTC directed to us. It won't matter much to us.

Those are decisions I cannot make.

The permanence of the CFTC, if you refer to that, we would like—we agree with——

Mr. GUNDERSON. I see that.

Mr. MELAMED. Yes.

Mr. GUNDERSON. Are you confident that the FBI investigation will not reveal any inadequate regulations by CFTC or any inadequate legislation regarding the whole futures industry?

I mean are you confident that there's nothing in the investigation that will reveal a need for change?

Mr. MELAMED. I would not say that I'm confident because I have no knowledge of what that will show. However, the little bit I have heard, and it is not with confidence that I say so, would not give us the indication that our surveillance system is not good.

Mr. GUNDERSON. And you don't anticipate anything from that investigation on the issue of dual trading?

Mr. MELAMED. I don't know. But I don't think that that is the only focal point or that it will be a main focal point. I don't expect that.

Mr. GUNDERSON. The one area that I am concerned about, as we look at a permanent reauthorization is the whole area of international trading.

You mentioned in your testimony at length on Globex, et cetera. Would you comment on Chairman Gramm's testimony earlier where she had obviously advocated giving them the authority to make investigations for foreign exchanges?

Would you believe that, as appropriate, No. 1, do you believe they have the resources and expertise, No. 2, to do that? And I would like you to be brief so I can pursue some questioning further.

Mr. MELAMED. Well, to the degree we have to give the CFTC the authority to do this kind of investigation, because it often leads to impact on our markets and our prices. We have to know that the integrity on the playing field of our customers in foreign lands is such that they are safe there as well. And the only way that can be done is if the CFTC has some authority to do those kinds of investigations.

Mr. GUNDERSON. Can you give this committee any examples where present regulations impede our competitive ability with other exchanges, such as Tokyo, London, et cetera?

Mr. MELAMED. Present regulations?

Well, the biggest problem we have faced is in authority to launch a new instrument. This requires authority from the CFTC that goes through quite a protracted period of review. And sometimes requires even a nonveto by the SEC.

I will give you an example of the kind of thing we've run into that has given me gray hairs.

It was with the Nikkei 225 stock index which represents the Tokyo stock market. When Clayton Yeutter, who is presently Secretary of Agriculture, was president of our exchange, and I achieved North American contract rights, with the owners of that instrument, the Nihon Keizai Shimbun organization of Japan we wanted to launch that instrument in our futures market in Chicago.

To do that, we applied to the CFTC. And we had to get a nonveto from the SEC.

Four years went by before that was achieved. By then, the Nikkei contract was listed in Tokyo and in Osaka. The stock index futures market began there. We still haven't listed it because we lost the right timing and, to a degree, we lost the market.

Mr. GUNDERSON. How many of your traders also would participate in say the Tokyo, London, or any other foreign exchange?

Mr. MELAMED. Well, it would develop. I do know in the beginning it would be probably small. But it will develop over time, and that's why you need the timing to institute the market so that it can increase in use and development. But I don't know in absolute numbers.

Mr. BRODSKY. I would supplement that by saying that the major firms that belong to our exchange have joined the Tokyo Stock Exchange and the Osaka Stock Exchange so they could trade these products. Because if they're offered there and not offered here, they will participate over there.

Many of the major investment banking firms and trading houses of the United States belong to the Tokyo Stock Exchange for that reason.

Mr. GUNDERSON. Are there varying degrees of standards for participation today in one exchange, here say versus the foreign exchange?

Mr. BRODSKY. There are very differing standards and, in fact, that's an area in terms of international trade policy that we have been involved in. Because there's been what I would call some discrimination against U.S. firms becoming members of offshore exchanges, where we have not had similar barriers. That's an area where we need the understanding and support of Congress.

Mr. GUNDERSON. All right. Thank you.

Thank you, Mr. Chairman.

Mr. ENGLISH. Mr. Nagle has one question.

Mr. NAGLE. Just one question for the record.

We were talking numbers of violations, you know, the 4,369.

How many members are there that trade on the exchanges in a given year?

Mr. MELAMED. Oh, I would say on average, we have 2,700 members, but not all of them, of course, trade. Many of them just own the memberships and lease them out.

I would say there's an average of around 2,000 traders.

Mr. NAGLE. You are hitting less than 1 percent with violation? You're finding less than 1 percent violation by the traders per year?

Mr. MELAMED. That's right.

Mr. NAGLE. I didn't want to leave the impression that everybody on the exchange was engaged in hanky-panky or anything like that.

Mr. MELAMED. I thank you for straightening that out.

Mr. NAGLE. I also did not say that nobody was engaged in violative conduct.

Mr. MELAMED. Well, we know that too.

Mr. NAGLE. Thank you.

Mr. ENGLISH. Mr. Coleman.

Mr. COLEMAN. Let me ask briefly, Leo, questions about the S and P 500 contract and your experiment to ban dual trading from that pit. That was and is a continuing experiment?

Mr. MELAMED. Yes, it is.

Mr. COLEMAN. And the results, as you have put forward in the report of the special committee, are such that it basically hasn't had an impact on the liquidity of the market.

Mr. MELAMED. Well, let me explain a little bit about that.

We didn't actually ban dual trading in that pit. What we did was exclude dual traders from the top step where the order flow comes. Therefore, by doing that, if you want to be a broker on the top step, you can't be a dual trader.

We know that most of the orders in the pit come from, through the top step. We expect that somewhere at the 90-percent level means that the brokers who handle these orders cannot trade for their own account.

While we did state that the impact, we have not measured as a result of the dual trading prohibition, we are not totally confident, because volume did fall precipitously since the time of the prohibition.

However, you will know that at the same timeframe, the 1987 stock crash occurred, and that too was a factor in reducing volume.

So it is difficult to make a concrete judgment how much effect was from one thing and how much effect from the other.

The experiment has given us some confidence but not total confidence.

Mr. **Coleman**. Is it something that we would want to take a look at as a possible legislative alternative to current bills and proposals?

Mr. **Melamed**. The top step exclusion is an old idiosyncracy of that market and isn't very transferrable to other markets. We considered that kind of thing ourselves and studied it. But it doesn't work the same.

See, most markets have different idiosyncracies and the order flow is different in each market. And so you really have to make that applicability in a market by market basis.

Mr. **Coleman**. Thank you.

Mr. **English**. Thank you, Mr. Coleman.

Leo, I have only one other question to ask you.

In listening to what you said and looking at what you presented, is it basically your perception that the difference between what the bill is before us and what you're proposing is we're talking about degrees?

Mr. **Melamed**. We are talking about degrees and the approach. Our approach is a standard of verifiability. The approach being submitted to us is a number of volume. That's a difference.

And then we're talking about whether you can do a complete 100 percent verifiability or some lesser reasonable number.

Yes, to a degree you're right. Our goals are certainly the same. The approach is somewhat different.

Mr. **English**. So basically we're talking about whether it's 90 percent or whether it's something higher than 90 percent. And the question is: How do we determine this question of liquidity and whether it should be done by volume or whether it be done by some other mechanism, is that right?

Mr. **Melamed**. That's right.

Mr. **English**. All right. Thank you very much, Leo. I appreciate your testimony.

Mr. **Melamed**. Thank you. I appreciate this opportunity. And I thank you for your work today. I know that it has been a difficult job but a very good one you have done. And we commend you for it.

Mr. **English**. Well, we want to keep working at it. You know, the objective of this legislation is to make sure that we substantially raise the standards up to what we expect in the industry. I know that's an objective that you agree with. It's one that I think will enhance the markets. It would certainly, I think, bring more confidence as far as the public is concerned in the markets.

And I think that's where they go for everyone, and it's for the good of everyone.

Mr. **Melamed**. Our goal is common. Thank you.

Mr. **English.** We are going to be looking forward to working with you.

Mr. **Melamed.** Thank you.

Mr. **English.** Thank you.

Our next witness is Mr. Robert Wilmouth, president of the National Futures Association.

STATEMENT OF ROBERT K. WILMOUTH, PRESIDENT, NATIONAL FUTURES ASSOCIATION, ACCOMPANIED BY DAN ROTH, GENERAL COUNSEL, AND JEAN TIPPINS, VICE PRESIDENT IN CHARGE OF ADMINISTRATION

Mr. **Wilmouth.** Thank you, Mr. Chairman.

And with your approval, I have two of my associates with me at the table. On my right is Dan Roth, who is our general counsel, and on my left is Jean Tippins who is our vice president in charge of administration.

And we thank you for the opportunity to present our views this afternoon.

As envisioned by Congress, NFA never intended to duplicate and has not duplicated the regulatory efforts of the exchanges. That is, the regulation on the exchange trading floors. Rather, our responsibilities to protect the public begin well before and continue well after the execution of a trade. Our members are the firms and individuals that conduct futures business with the public.

Just quickly, our four primary responsibilities include the following:

One, preventing unethical firms and persons from entering or conducting business in the futures industry. We do this by performing a screening and registration function on behalf of the CFTC;

Two, we try to assure that those who do conduct business in the futures industry do so according to high ethical standards. They must comply with the rules which we have developed and which we strictly enforce to protect the public customer;

Three, we do provide through our extensive education programs the information that can help the public make informed investment decisions or, depending on the individual, an informed decision not to invest in the futures market; and

Four, we have established a nationwide arbitration forum that provides public customers with a fair, prompt, and inexpensive means to resolve any disputes which may arise in connection with the trading of futures contracts.

Our accomplishments in each of these areas since the last reauthorization of the CFTC are described in a report which we have provided to each of you.

Now, certain proposed amendments to the act would directly impact NFA in carrying out its responsibilities. And it is those on which I would like to comment specifically today.

There are some others which do not directly impact NFA but, of course, would have a profound impact on the futures industry, and my comments on those areas are contained in my written testimony. But specifically to those that affect NFA:

One is registration requirements. One of the best ways to protect the public from unscrupulous firms and individuals is to keep those people out of the industry in the first place. NFA has been handling this job since October 1, 1985, when we assumed responsibility for denying, revoking, restricting, or conditioning registration for all categories except floor brokers and leverage transaction merchants.

We strongly support the proposed amendments which will not only fine tune and tighten the fitness standards of the futures industry, but would codify certain of the Commission's and NFA's prior interpretations of the existing disqualification provisions and resolve certain ambiguities in the act which NFA has encountered over the past 4 years.

Furthermore, should floor traders, as your bill provides, be required to register under the act, we have the capability to perform that activity.

On the subject of telemarketing fraud, the prevention of deceptive sales practices is precisely where NFA has focused its rulemaking and rule enforcement efforts. We believe this industry's sales practice regulations are second to none in their comprehensiveness, effectiveness, and enforcement. Thus, while we welcome any legislation which would help combat whatever small percentage of persons in our industry who engage in deceptive or high pressure sales tactics, we have serious reservations as to whether the proposed legislation would in fact have that effect.

The proposed rule could unduly be burdensome to the overwhelming majority of our members who are honest, legitimate business persons. Correctly identifying which "first time" customers are solicited by phone could pose substantial problems of practicality in the real world. In addition, there may be sophisticated institutional customers whose trading may not be exclusively hedging for whom this "protection" would be both unnecessary and potentially harmful.

If there is any way to narrow the focus of this concept, to pinpoint the relative handful of unscrupulous firms, NFA could support the proposal and, in fact, we do have some ideas which we would like to present to the committee.

With respect to the issue of public representation on our board of directors, our articles of incorporation have always provided for public representation. Three of the 42 people on our board are elected as public representatives, and their varied backgrounds provide a wealth of industry, legislative, and academic perspectives. But we also have five other members whom we believe qualify as public directors. Three of those represent commercial firms, and the others represent commercial banking institutions. And they give us valuable external insights and counsel.

So if we understand correctly, we are already in substantial compliance with your requirement of 20 percent since 8 of our 42, or roughly 19 percent of our seats, are covered by what we call public members.

The issue of disqualification standards to serve on NFA's board of directors and disciplinary committees is one which we are currently considering, and we think it may well be appropriate to disqualify from board or committee membership persons who have been found to have committed a major rule violation.

We would caution the committee, however, that in determining what constitutes major rule violation, the focus must not be on the rule but on the violation. All of our compliance rules are designed in one way or other to protect the public. The violation of any of these rules could so undermine one's confidence in a person's judgment that he should be disqualified from board membership. Others, however, may only be technical in nature. And the best way to determine a major rule violation is to focus not on the rule that was violated, but on the sanction.

If that reflects the committee's intent, we certainly support the proposed amendment.

We also agree with the committee that registrants should receive adequate trading concerning their ethical responsibilities to customers. Toward that end, we have already made significant changes in the National Commodity Futures exam. The content has been changed to put greater emphasis on an understanding of regulatory requirements, and the exam is graded not only on market knowledge but equally so on regulatory knowledge.

And while these changes have already improved the industry's attention to ethics training, we fully support any proposed amendments which would focus even greater attention on this critical area.

And, finally, NFA strongly supports the proposal to make the CFTC a permanent agency. This would ensure continuing congressional oversight of the CFTC, it would eliminate ongoing uncertainties about the agency's existence, and it would facilitate more effective use of the Commission's resources to regulate futures markets. The proposal is both welcome and long overdue.

Again, we thank you for your attention, and we will be pleased to answer any questions that you might have, Mr. Chairman.

[The prepared statement of Mr. Wilmouth appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Bob. I appreciate that.

There has been a good deal of discussion with regard to the question of how we do the telephone solicitation. I know that this committee is not the only committee that has an interest and is concerned about that. And we are looking for ways to strengthen that particular aspect of it. The real question comes down even with the 3-day period that we have after a person is registered.

They file or apply with a firm. Even then we are concerned that the unscrupulous may find a way to maneuver around that particular aspect.

Do you have any specific suggestions as to how we might address that?

Mr. WILMOUTH. Well, we have several thoughts, and I might ask Dan Roth, our general counsel, who has been looking at this, as we thought that might be a possibility to discuss some of the ideas that we do have. And we would like to present them later in detail to you.

Mr. ROTH. Just in general, I think the two points to be addressed are the effectiveness of the proposal and its unintended side effects.

With respect to unintended side effects, just two points we would note in passing, that we would be happy to discuss with staff at greater length.

We might be able to draw some comparisons from NFA's own "know your customer" rule. For instance, that rule, which has proved a very effective enforcement tool for NFA, applies only to customers that are natural persons and not to corporate customers and, therefore, limits the scope of the people that are entitled to the protection from that rule to those people that need it.

Any investor sophisticated enough to incorporate is arguably sophisticated enough not to need the protection of NFA compliance rule 2-30. The same point might be made with respect to a proposed telemarketing fraud provision.

Similarly, our rule requires members to gather certain information from customers such as their net worth and annual income and so forth. The rules makes very clear so as not to be unduly burdensome on our members, that our members can rely on the information provided to them by the customers, and have no due diligence obligation to try to verify or corroborate that information.

A similar type provision for this aspect of the bill regarding whether a customer is a first time customer and whether he was solicited by phone is something that might want to be considered.

In addition, we would like to talk with staff about possibly pursuing this as a means of refining the supervision requirements which are already incorporated into CFTC rules and NFA rules. Clearly what constitutes diligent supervision will vary from firm to firm depending on the nature of the firm's business. For those firms more actively engaged in retail sales, for those firms which have past disciplinary histories, for those firms whose sales forces have come from firms with disciplinary problems, it may well be appropriate to impose upon those firms somewhat different provision requirements. That might be a way to focus the attention of this provision.

Mr. ENGLISH. Mr. Roth, it sounds like that would be an area that we would be very interested in so I hope that you will continue to work on that and consult with both majority and minority staff on the subcommittee.

We are looking for a way of refining down that particular aspect of the proposal. So that would be most helpful and, Bob, we would appreciate that very much.

Mr. Coleman.

Mr. COLEMAN. Bob, let me ask you a question about your new procedures to review promotional material for members.

I believe you have embarked on a pilot project or a program the beginning of May in which people can run materials by an NFA committee and get an approval based upon some facts, which would have to be documented eventually.

You could give an overall approval, a disclaimer, and help basically your members who are trying to conform to the appropriate NFA rules.

If a company does that, comes to you and your review panel, and you give them the approval, do they basically have a defense that you can't come back later, having depended upon that approval and cite them? That's kind of like what we hear from constituents with the IRS. They get misinformation and the IRS says, oh, I'm sorry, that was misinformation, even though the agency gave it out.

What is your position on that?

Mr. **Wilmouth.** Let me go into a little bit of background, if I can.

The question of what constitutes proper advertising and what doesn't has been one that our members have been concerned about because what they think they're doing is correct, and then we come along and we slap them with a fine, or we suspend them, or something like that.

What we have attempted to do is to say to them, look, if you submit your advertising to us in general, we will take a look at it, and we will tell you whether or not we think it's going to comply with our rule. We are going to do that within a period of 3 weeks, and this is on a trial basis.

It would be my feeling that it would not necessarily, and I may have to refer to legal counsel, would not necessarily exempt them from any punishment from us if we found out later on that they had twisted it.

But if somebody comes in and presents a piece of advertising and we say that it looks OK, and it continues to be used in that exact same format, I would think we would have a difficult time of proving that it was wrong if we had put our blessing, our stamp of approval on it.

But essentially it's just to give them a general overall approval of the approach they're taking.

Mr. **Coleman.** OK. Now, previously, under the old methodology, you would perhaps take what you might call a no action position. You would not approve in a positive sense but you wouldn't disapprove?

Mr. **Wilmouth.** No. What we used to do before was to require certain firms with whom we had a problem to submit their advertising to us in advance. We made that a specific requirement. If we did an investigation of a firm and we brought them to the attention of our business conduct committee because of the fraudulent advertising that they were using, or the misleading advertising, one of the sanctions might be you must submit that advertising to us in advance, and they would have to do that. Otherwise, they would be in violation of our order.

And this was to make certain that any of those who were a problem in the past had an opportunity to come in and present new material in advance and get kind of our imprimatur or blessing or seal of approval, "Good Housekeeping" seal of approval in a way.

Mr. **Coleman.** Would you indeed give your approval, or would you take a nonaction?

Mr. **Wilmouth.** No. We basically, if they submitted the advertising to us in accordance with our request, and we saw nothing wrong with it, we would let them go ahead and use that advertising.

Mr. **Coleman.** I see.

And what if it was not a problem firm that didn't get a request from you to submit this, what would be the normal course of the firm?

Mr. **Wilmouth.** If we felt it was serious enough, we would bring an action or a complaint against them, and bring it to the attention of our business conduct committee.

In many cases, I must say that when we bring that to their attention, they would stop using it immediately, and then there would be no new cause to go after it because it would be an honest misinterpretation of what they felt would be OK before we brought it to their attention. Then they would refrain from using it.

Mr. COLEMAN. But previously if the firm had not had problems, but had submitted something to you, you would have said——

Mr. WILMOUTH. We didn't have a program like that——

Mr. COLEMAN. You didn't have a program?

Mr. WILMOUTH. Until just recently. This is our new pilot program——

Mr. COLEMAN. So there was no way of doing it before?

Mr. WILMOUTH. That's right.

Mr. COLEMAN. And no one would have said, well, the fact that we are not going to approve this doesn't mean we are disapproving it either?

Mr. WILMOUTH. That's right. What we kind of felt as we got along, and you have got to remember, NFA is a relatively new organization, it began in 1982, we tried to put out some interpretive notices as to just exactly what we felt would be good or bad in a particular area.

And I think advertising is a very difficult one to do. And some of our members were effectively saying, we think that you're cracking down on us when you really shouldn't be. That's why we have devised this recent program.

I must also say that we spent a lot of time, particularly in our early years, and still do, assisting a lot of our members in terms of helping them not only set up books but also determining what is and what isn't proper advertising or proper activities with the customer.

Mr. COLEMAN. Thank you.

Mr. ENGLISH. Well, thank you very much, Bob. I appreciate your testimony and we are looking forward to working with you.

I think that one provision is an area that we can strengthen and we look for the help NFA can do.

Mr. WILMOUTH. I certainly will. We'll have something to you next week. Thank you.

Mr. ENGLISH. Let me also say that we have received letters commenting on this bill, and we expect to receive statements from a number of other organizations. Any statements, written statements that are submitted to the subcommittee will be included as a part of our record.

[The prepared statement of Ms. Vogel appears at the conclusion of the hearing.]

Mr. ENGLISH. We will now recess until 2 o'clock, when our next witness will be Mr. Karsten Mahlmann who is with the Chicago Board of Trade.

[Whereupon, at 12:55 p.m., the subcommittee recessed, to reconvene at 2 p.m., the same day.]

AFTERNOON SESSION

Mr. ENGLISH. The subcommittee will be in order. Our next witness is Mr. Karsten Mahlmann, who is chairman of the Chicago

Board of Trade, and I see that he has individuals accompanying him.

Mr. Mahlmann, we are going to let you introduce the gentlemen that are with you.

STATEMENT OF KARSTEN MAHLMANN, CHAIRMAN, CHICAGO BOARD OF TRADE, ACCOMPANIED BY THOMAS DONOVAN, PRESIDENT AND CHIEF EXECUTIVE OFFICER; DONALD ANDREW, MEMBER, EXECUTIVE COMMITTEE OF THE EXCHANGE; SCOTT EARLY, GENERAL COUNSEL OF THE EXCHANGE; FRED GREDE, VICE PRESIDENT IN CHARGE OF THE OFFICE OF AUDITS AND INVESTIGATIONS

Mr. MAHLMANN. Mr. Chairman, thank you very much for letting us appear before your committee to address H.R. 2869. With me this afternoon are, to my right, Mr. Thomas Donovan, president and chief executive officer of the Chicago Board of Trade; next to him, on the right, Mr. Donald Andrew, a member of the executive committee of the exchange, a member of the board; next to my left, Scott Early, general counsel of the exchange; next to him, Fred Grede, vice-president of the exchange in charge of the office of audits and investigations.

Mr. ENGLISH. I want to repeat what I said earlier this morning. Anyone testifying this afternoon and summarizing their testimony, without objection their full and complete written testimony will be made a part of the record.

Mr. MAHLMANN. Thank you very much, Mr. Chairman.

Mr. ENGLISH. So, we'll turn it to you.

Mr. MAHLMANN. Mr. Chairman, I am here to present the views of the Chicago Board of Trade on H.R. 2869, the Commodity Futures Improvements Act of 1989.

Among other things, this legislation makes the CFTC a permanent Government agency. The Chicago Board of Trade endorses that action. While we do not agree on everything with the CFTC at all times, we respect the important role played by a mature and expert agency in overseeing the self-regulatory scheme embodied in the Commodity Exchange Act. The vote of confidence reflected in H.R. 2869 for the CFTC is well-deserved.

Mr. Chairman, in sponsoring H.R. 2869, you indicated that you wanted to promote both the integrity of U.S. futures markets and our ability to compete with foreign markets. We share these objectives, but disagree with how some of the provisions in H.R. 2869 would accomplish them. We would like to propose alternative provisions that would accomplish the same objective of elevating industry standards.

The Board of Trade is committed first and foremost to maintaining the integrity of our markets. In the past week, we saw a demonstration of the depths of our commitment. As you know, on July 11, the Chicago Board of Trade took emergency action to remove the threat to an orderly liquidation of the July 1989 soybean futures contract. It took courage to take this action because we knew we would be criticized by some, but we acted, nevertheless, because of our commitment to preserving marketing integrity and because strong, self-regulatory medicine was needed. As Secretary of Agriculture Clayton Yeutter said, "The Board of Trade has nothing to apologize for. Preventive medicine is better than curative medicine."

As this recent episode shows, the Board of Trade will not hesitate to take decisive action when needed to maintain investor confidence. We welcome further discussion on the soybean issue at the conclusion of my testimony.

As a reflection of confidence in our markets, investors are participating in futures markets at ever increasing levels. Over the last 4 years, the Chicago Board of Trade volume has grown by 92 percent. During that same time period, foreign futures exchange volume increased by over 226 percent. Foreign countries are waking up to futures trading and to economic and social benefits that futures trading provides.

Even though U.S. futures industry volume has increased over the last 4 years, market share has decreased by 10 percent. Foreign futures exchanges now account for 30 percent of total futures volume for exchanges gained in market share exclusively at the expense of U.S. futures markets.

U.S. exchanges do not have a monopoly on the products they trade. The Board of Trades most active product, U.S. Treasury Bonds, is now listed for trading in London, Sidney, Singapore, and will be traded later this year by the Tokyo Stock Exchange. The Chicago Mercantile Exchange's most successful product, Eurodollars, is traded in London, Singapore, and now the Tokyo Financial Futures Exchange. Our products and our success are the envy of the world.

Why do we cite foreign competition? Many industries have come before Congress to ask for protection from foreign competition. We seek no such protection. We ask only that you not inhibit our ability to compete with these growing markets. The U.S. futures markets are already the most heavily regulated in the world.

We recognize the competition facing U.S. financial markets. In the Far East, virtually unlimited capital is available. At the same time, European countries are uniting economically to develop a true common market in 1992. The European community recognizes the formidable economic position of its international competitors, and is taking steps to meet those challenges.

Faced with these trends, the U.S. futures industry has taken measures to strengthen our markets in a cost efficient way. In today's environment, we are attempting to create a unified front to manage our future direction.

The Chicago Board of Trade and the Chicago Mercantile Exchange recently announced that discussions would begin in an attempt to unify Globex and Aurora, the computerized trading systems developed by each exchange. By creating a unified trading system, we believe that we can lower the cost of doing business to market participants, making us more competitive with the rest of the world.

The Chicago Board of Trade and the Chicago Mercantile Exchange recently also agreed to unify their electronic audit trail, the Computerized Trade Reconstruction System, combining the best of the Board of Trade system with the best of the CME's approach, creating the potential for an industrywide standard.

In addition, the Board of Trade and the Mercantile Exchange have agreed to unify their existing computerized surveillance programs, CATS by the Mercantile Exchange, CTR Plus by the Board of Trade.

The unified system will review 100 percent of trading activity at both exchanges. No trade will escape the exchanges' computerized microscope. As a result, both exchanges will operate a new and improved audit trail and surveillance to detect those trading violations that are attributable to dual trading as well as other types of potential trading abuses.

Moreover, the subcommittee should not lose sight of the fact that the existing Board of Trade audit trail and surveillance capabilities already meets the highest standards. As U.S. Attorney Anton Valukas has publicly stated, "They—the Board of Trade—have the resources to identify trading practices in which fraud has occurred."

The Board of Trade has already passed new regulations in a number of areas. Our audit trail is becoming tighter with new time stamping systems and narrower timing requirements. Computer surveillance has been upgraded. Surveillance personnel have been increased by more than 30 percent in order to adequately handle the task at hand. New rules and broker associations and opening and closing procedures have been passed. Both the Board of Trade and the Mercantile Exchange are implementing new technological innovations, including the advent of electronic audit delivery systems which will insure that customer orders have the most accurate audit trail possible.

In summary, the Board of Trade already has taken steps to insure enhanced customer confidence in our markets which will strengthen our ability to provide liquid and fair trading markets to the world.

As I mentioned earlier, we support many provisions in H.R. 2869. We applaud the legislation's primary objective to insure good, clean, honest markets. However, we recommend that certain provisions be modified in order to permit the efficient functioning of U.S. futures markets to continue.

First, we oppose the provisions in H.R. 2869 that would ban dual trading. We believe there is a way to preserve the benefits of dual trading while also protecting against a potential for abusive trading practices. This proposal eliminates the benefits of broker trading without considering the cost inherent in doing so. We strongly recommend that a cost benefit analysis be prepared regarding the specifics of this proposal before it is legislated.

Mr. Chairman, I think we can all agree that dual trading, per se, is not bad. In fact, dual trading contributes significantly to market liquidity. What is bad is when brokers front run customer orders to gain a financial advantage. To address that misconduct, the Board of Trade and other exchanges have had rules on their books that prohibit brokers from trading ahead of customer orders. Any member violating that prohibition faces a full range of exchange-imposed penalties from substantial fines to expulsion.

Moreover, any approach to the topic of dual trading must be consistent and comprehensive. This proposal only addresses floor trading. The Presidential task force on market mechanisms, known commonly as the Brady Commission, found that "the markets for stocks, stock index futures, and stock options are in fact one market." Therefore, to address the dual trading question properly, a review of all dual trading on exchange floors and off exchange floors both in futures and securities as well as the ultimate dual trader—the specialist—should be required. As currently provided, this proposal does not foster a level regulatory playing field. Off-floor dual trading would permit an FCM or its employees to front run customer orders. Nothing in this proposal addresses this possible abuse.

Demonstrating another inconsistency in this proposal, the CFTC, on Monday of this week, approved the trading of commodity SWAPS without any Government oversight. SWAPS are direct substitutes for futures contracts. Those who engage in commodity SWAPS will be permitted to dual trade completely outside the regulatory oversight of the CFTC or of this committee. H.R. 2869 will not touch this unregulated market where dual trading will occur regularly.

The proposal to ban dual trading will adversely affect the liquidity of futures markets, particularly so, agricultural markets, by increasing the cost of doing business. The pricing impact on U.S. agricultural futures markets will also adversely impact the pricing of physical agricultural products traded in this country.

We recognize that H.R. 2869 includes certain exemptions from dual trading prohibitions designed to permit flexibility for the CFTC on a contract-by-contract basis. In effect, however, before the CFTC can use these powers, the markets must be illiquid and potentially irreparably harmed.

H.R. 2869 also exempts any Board of Trade from the trading prohibition if its audit trail is fully verifiable and can detect any and all abuses. However laudable, this standard is unattainable in the real world. The imposition of this perfect standard would bring our business to a halt. We believe that a more realistic approach would be to exempt any Board of Trade from the dual trading ban if the CFTC concludes that the Board of Trades audit trail and surveillance systems provide for the effective detection of statutory and regulatory prohibitions.

With respect to the audit trail proposal, we again find the objective of the bill's drafters laudable. No exchange in the world has demonstrated a greater commitment to the implementation and usage of advanced technology in its audit trail system. In the absence of a definition of verifiable, we believe a 30-second standard should be a goal since it is not achievable with current technology. We suggest a more flexible approach which would permit the exchanges to work with the CFTC to research and develop technological enhancements to the audit trail rather than legislating standards.

Finally, with respect to make-up of disciplinary committees, the current proposal, contrary to the fundamental premise of our system of justice would dictate that an accused member not be tried by a jury of his peers. Disciplinary hearings are extremely serious matters. This proposal severely affects the rights of the individuals involved. As U.S. Attorney Anton Valukas recently stated, "In my estimation, based on my own expertise in the area, the best experts in the world concerning trading practices are the members of the Board of Trade." This statement was made while the alleged undercover investigation was supposedly going on.

In summary, Mr. Chairman, we can endorse many provisions in this bill, but others may have serious and irreparable adverse ramifications on the liquidity, pricing, and operation of U.S. futures markets.

We will be happy to work with this committee to develop effective legislation for the regulation of U.S. futures markets. We share this committee's concern to uphold the integrity of our markets and maintain continued customer and investor confidence. We must stress to this committee that the U.S. futures markets are the best regulated in the world, and as such are the envy of our foreign competitors. We cannot afford to hand our markets to those competitors. Unless we are careful in the crafting of this bill, we will tilt the regulatory playing field in their direction.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Mahlmann appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Mr. Mahlmann. I appreciate that.

It would appear, in going through, I was taking note of the fact that it would appear, with the exception of the disciplinary committee question, that the general disagreement—generally speaking—the disagreement with this legislation has more to do with degrees than it does with regard to the objective itself, the question how far can we go, how much can we accomplish.

Would you agree that that is the basis for the disagreement at this point?

Mr. MAHLMANN. Mr. Chairman, as I have stated in my written testimony that I just read, we wholeheartedly agree with the goal of the committee and with the proposal in the bill. It is a question of degree and how do we get there without impacting the liquidity of the marketplace, but at the same time detecting virtually all abuses; "any and all," that's difficult.

Mr. ENGLISH. Let me speak to that at this particular point. The provision of "any and all" is subject to definition. I think the real question is the issue of whether this legislation is going to encourage through a carrot and stick approach, and many within in the futures industry have stated that they thought that that approach is a proper one, the question of how far can we go, what kind of standards can we expect.

This subcommittee has not, and of course we will as we move through the legislative process define exactly what that means. We deeply appreciate and look forward to working with the Board of Trade in reaching a definition that quite frankly is ambitious but by the same token obtainable.

So, we do look forward to working with you on that, and we appreciate the offer of helping us in that matter, and we will be calling on you without question on that. So that is deeply appreciated.

Let me state that there have been a number of questions with regard to the issue of the action taken last week by the Board of Trade pertaining to soybeans. I have two questions. The first one is the question given the existing situation in the market—in the soybean market—is it possible that the Board of Trade may have to take some more action next month?

Mr. MAHLMANN. Mr. Chairman, the Board of Trade, through its committees and through its staff in the office of audits and investigations is daily monitoring the August contract which is now the nearby delivery month. I strongly hope, as the chairman of the exchange, that similar action will not be necessary.

Mr. ENGLISH. But it cannot be ruled out.

Mr. MAHLMANN. I cannot state that it will not be.

Mr. ENGLISH. OK, that is very good. I appreciate that.

The next question is one that we addressed to the CFTC when Chairman Gramm appeared before us on Tuesday, and that gets into the question of the decisions or the action that led up to this decision and the involvement of the CFTC. As the law stands now, of course the CFTC has the authority, should they disagree with the action of the Board of Trade, to overrule that action, but there is nothing in the law as it stands now for the CFTC to, in effect, respond in the affirmative unless they so desire.

Several members of this committee made the point, and I think rather forcefully, that given the fact the CFTC was notified in advance of this decision being announced that no statement, no response is tantamount to approval, and I think there is a great deal of interest in this subcommittee as to exactly what involvement the CFTC had in the decision, and what was the interaction between the exchange and the CFTC on finally reaching this decision.

Could you give us an overview of exactly, and in as much detail as possible, what the interchange, the interrelationship was between the CFTC and the Board of Trade?

Mr. MAHLMANN. Mr. Chairman, if I am permitted to step back for a moment in time, I will go back to approximately the first week of June. We had just come through a May expiration that we all were very happy that had got done by the skin of our teeth, but it did get done without any emergency.

Even through that time, we were in daily contact, and from then on forward, with regard to the July contract, we were in daily contract with the Commodity Futures Trading Commission, both at the staff level and from chairman to chairman, and there was intimate dialog, going on into the emergency action that the Board of Trade took from myself to Chairman Gramm on an almost daily basis.

Mr. ENGLISH. With this interaction, this daily contact between you and the chairman and between other members of the Board of Trade, and I assume other members of the staff of the CFTC, perhaps other Commissioners, did the Board of Trade at any time make any recommendations or did the CFTC make any recommendations to the Board of Trade contrary to the decision that the Board of Trade took?

Mr. MAHLMANN. Mr. Chairman, the CFTC arrived independently of the Board of Trade on the same day at the identical conclusion that the Chicago Board of Trade Board arrived at in its special board meeting of the afternoon of July 11. The CFTC, independently of the exchange, determined that there was a threat to orderly liquidation of a contract, which is the same foundation that—and the same decision that the Board of Trade board arrived at on the afternoon of July 11.

The actions that were then taken by the two parties vary to some degree and are identical to another degree, if I may elaborate.

Mr. **English**. Please do.

Mr. **Mahlmann**. The Commission in coming to the decision that a threat of orderly liquidation existed came to the conclusion that it notified a single market participant that effective the close of 3 days before the expiration of the contract its anticipatory hedge exemption from speculative limits would be revoked.

Putting it into plain english, it said the major market participant on the long side, singly by himself had to come down to 3 million bushels as of the close of the 18th. The Commission so notified the market participant.

The Chicago Board of Trade board, on input and advice, and seeking of help from the business conduct committee, addressed the same issue on July 11 at 2:15 in the afternoon. The Chicago Board of Trade board independently reached the conclusion that there was a threat to the orderly liquidation of a contract, that if it was not addressed could lead to the potential default of the contract.

The Board of Trade board then, in its order, acted across the market, meaning market neutral, not against a single participant but market neutral against all market participants insofar as anybody that held in excess of 3 million bushels, whether it was hedge or not, was not the deciding factor, was not a material factor. The concern was orderly liquidation.

Therefore, anybody with positions in excess of 3 million bushels had to reduce those positions in a gradual step way, 20 percent per day, down to a figure of no more than 3 million bushels as of the close of July 18.

The end position on July 18 in the Board of Trade's order and the CFTC order are identical. The Board of Trade's order applied to all market participants, whether long or short. The Board of Trade's order incorporated gradual steps. The Board of Trade's order was taken ever mindful of our obligation to have orderly markets, and particularly so, orderly liquidation, and it did not address a single market participant.

The Board of Trade order, in its final step, at the expiration of about 45 minutes ago, also included a provision that no market participant could go off the board, meaning, have a position open after the final bell of trading in excess of 1 million bushels.

But yes, both parties, regulator and the market, took independent actions along the same lines.

Mr. **English**. Mr. Coleman.

Mr. **Coleman**. I am going to go over the same ground a little bit with you for emphasis. First of all, this intimate communication that occurred between the Exchange and the Commission started back in early June; correct?

Mr. **Mahlmann**. Congressman, it started before that on the May contract. With regard to the July contract, in early June, yes.

Mr. **Coleman**. In early June. And was that primarily conducted between you as chairman and Dr. Gramm as chairman, or were others involved?

Mr. MAHLMANN. The staff of our office of audits and investigations and the staff of the Commission were as well in daily contact.

Mr. COLEMAN. And during such periods of time, do you feel and is there a confidentiality issue involved to the extent that you do not share that information with others?

Mr. MAHLMANN. There is very much a confidentiality issue involved. Our office of audits and investigations is ever mindful of that obligation that they have as staff members of the exchange, and so am I as chairman.

Mr. COLEMAN. So I would take it that other than yourself, there was no other board member who was involved with or familiar with or was related to any information regarding this?

Mr. MAHLMANN. The only participants knowledgeable in the dialog were the two gentlemen sitting to my left: General counsel of the exchange and vice president of the audits and investigations department. No board member was knowledgeable.

Mr. COLEMAN. I am sorry? No?

Mr. MAHLMANN. No board member was knowledgeable.

Mr. COLEMAN. Now, the CFTC—I am not sure what we are going to call this. The CFTC informs a major participant, your statement said: Was that through an informal proceeding, to your knowledge, or was there an order issued? How would you characterize this communication?

Mr. MAHLMANN. They directed the major participant in writing that his previously granted hedge exemption would be revoked for the last 3 trading days of the July contract.

Mr. COLEMAN. Did they inform you of this action prior to its being taken?

Mr. MAHLMANN. No. They informed me after they had taken it.

Mr. COLEMAN. Had you been in discussion with them about a possibility of some action being taken, and was this one of the alternatives that had been discussed?

Mr. MAHLMANN. Congressman, we had been in daily discussions of what alternative steps could be taken. They did not discuss what they would do with me.

Mr. COLEMAN. Under the circumstances, and while this is an unusual circumstance, is it your feeling or is it your opinion that the Commission was to give the exchange the first right to move in such a case? Or do you feel that you—I mean, who was waiting for whom to move here? I guess that's the question.

Mr. MAHLMANN. Congressman, I have to take you back to the chronological event of how the last occurrence occurred. Within the exchange, the monitoring of orderly markets, and particularly so the monitoring of an expiring futures contract, is delegated to the business conduct committee. The business conduct committee is a sworn-in committee by oath to keep the secrecy of any item that came before them on any issue, and they standardly go through the procedure of recusal, and having been asked for a recusal if there is any party involved in a particular commodity.

That committee has been continuously monitoring the July contract. At various instances through the month of June and into July did this committee call in market participants, both long and short, and reminded them of their obligation to effect orderly liquidation of a futures contract. At the last meeting prior to the decision, the business conduct committee instructed a major participant that, under its obligation to orderly liquidate positions, it would have to do so on a daily basis in a reasonable fashion. And the committee told the major market participant—and this meeting occurred on July 6 and was followed up by a letter of those instructions on July 7—that the committee would deem 3 million bushels a day reasonable liquidation.

The committee also notified the major market participant if the participant would not abide by the guideline and directive given to it by the business conduct committee, the business conduct committee, seeing that it had no powers themselves to effect liquidation within the rule structure, would have to present to the board the case that they deemed emergency action in order to ensure orderly liquidation would be necessary.

The business conduct committee monitored for 2 days the action of the major participant, and when they did not find adherence to the proposed guidelines that they had given—meaning 3 million per day liquidation—at that point the business conduct committee recommended to the board to take emergency action.

Mr. COLEMAN. Well, my question is: Should there be some sort of structured process by which the Commission on its own not only could have but should have made these decisions and acted prior to what you have just related to me by the exchange?

Mr. MAHLMANN. Congressman, I believe that the exchange, being intimately involved in the marketplace and monitoring on a daily basis, is a better judge of whether an emergency exists or not.

Mr. COLEMAN. And even though the Commission had concluded the same thing, how did they conclude that, other than based upon information that you gave them?

Mr. MAHLMANN. Congressman, I can comment on the Board of Trade's conclusions. I cannot comment on the Commission's conclusions of how they arrived there.

Mr. COLEMAN. But any information that they received would have had to have been relayed by you? Or how would they have determined that?

Mr. MAHLMANN. Congressman, I presume the Commission and its staff also draws its knowledge from independent sources.

Mr. COLEMAN. And when we have an information letter, I guess we will call it, from the CFTC that basically required this major market participant to do the same thing that you ordered them to do: What is the difference as far as the effectiveness goes of what a Government commission tells somebody to do—which apparently they were not paying attention to because you had to then follow up with some sort of action on your own? Is that correct?

Mr. MAHLMANN. The two actions occurred independently of each other on the same day.

Mr. COLEMAN. On the same day.

Mr. MAHLMANN. Yes. But with respect to your comment on the difference of the two actions, why did we have different actions, the Board of Trade's action applied equally across the market. The Board of Trade's action also incorporated a gradual day-by-day 20 percent reduction requirement. The potential of the Commission's action would have been that the major market participant, out of 23 million bushels—and I can mention the figure because it was stated in public court—might have elected to sell 20 million bushels on 1 day. I have no idea what that impact would have been on the marketplace.

Mr. COLEMAN. Well, is this an informal rule as far as having the participant know that they are going to have to liquidate their position? Is there an exchange rule, or is this an informal rule?

Mr. MAHLMANN. The Commission has its own rule, and the Board of Trade has its right in its charter and bylaws under emergency action.

Mr. COLEMAN. That is your authority?

Mr. MAHLMANN. So both parties have the authority.

Mr. COLEMAN. Yes. Well, the story in this morning's Wall Street Journal characterizes this as a violation of an unwritten rule of the Board of Trade. Is it, in fact, an unwritten rule, or is it a written rule?

Mr. MAHLMANN. The Wall Street Journal must be referring—and I can only speculate on that—to the job awning which is the only thing that the business conduct committee can do. The Board itself under rule 180 of our exchange has the emergency powers rule that can mandate market participants what to do in order to achieve orderly liquidation of a contract, which is in turn demanded of us under the Commodity Exchange Act.

Mr. COLEMAN. All right. Thank you.

Mr. ENGLISH. Mr. Combest.

Mr. COMBEST. No questions.

Mr. ENGLISH. Mr. Tallon.

Mr. TALLON. Mr. Chairman, thank you.

Mr. Mahlmann, I believe you testified that 100 percent audit trail that would detect any and all abuses would be an impossibility for you to have in place, that kind of audit trail.

What is your accuracy rate with the audit trail that you have at that Chicago Board of Trade now?

Mr. MAHLMANN. The last CFTC review and substantial steps have been taken since then indicate that the CFTC finds the Board of Trade audit trail or the logic that leads to the Board of Trade assignment of times in its audit trail that it could presume an 88 percent accuracy.

Mr. TALLON. The liquidity with the banning of dual trading when a contract reaches a volume of 7,000 contracts on a daily basis, the threat to liquidity which brings more stability to the market is certainly something I am concerned with.

Is this 7,000 volume in a contract? Why isn't that a mature liquid contract when you reach the 7,000 volume?

Mr. MAHLMANN. Congressman, I cannot tell you when a contract is mature and when it is not mature. I have never heard any criterion used on that before.

What we had proposed because we embraced the committee's goal of getting to good clean, honest market that substantially detect virtually every abuse that there is. The exchange just approached, if it can offer that to the committee, would be that an audit trail through computer technology and surveillance systems through computer technology that reach as a nearby goal a 90 standard and then as additional technology becomes available that

that goal be increased, that that be the measure rather then the contract volume.

Contract volumes change. One contract can be liquid today, illiquid tomorrow. We think that is a better implementation rather than taking the liquidity which dual trading prevents out of a marketplace.

Mr. **TALLON**. You think you could reach a 90 percent accuracy rate in 18 months?

Mr. **MAHLMANN**. I strongly believe so.

Mr. **TALLON**. You mentioned off-floor dual trading. I guess you were talking about people like a futures merchant or brokerage house receiving orders. Certainly in the securities market, certainly specialists on the New York Stock Exchange. I believe you said they were the ultimate dual trader in the things that we would have jurisdiction over or direct the CFTC to look at.

What kind of job in just those areas like a futures merchant where orders come into brokerage house, what kind of job has this bill done in addressing any possible or potential abuse of dual trading?

Mr. **MAHLMANN**. Congressman, it is my feeling that this bill has singled out on-exchange dual trading only. It has not addressed dual trading if it is taken in the same vein as a broker trading for himself and for his customer. That can occur off-exchange, that can occur in the futures industry, that can occur on the securities industry, that can occur upstairs on private trading desks, and that can occur on the New York Stock Exchange within the specialists, and it can occur not only in the CFTC regulated industry, it can occur in the SEC regulated industry.

So my view is that H.R. 2869 only addresses this on exchange floors while leaving all the other industries untouched in its auditorial requirement, and I submit to this committee that would put exchange floors on a tougher standard than either another industry or any other part of the industry.

Mr. **TALLON**. Are you saying that maybe even a real estate broker is a dual trader or an insurance agent or a banker?

Mr. **MAHLMANN**. They all can be.

Mr. **TALLON**. How many people do you have authorized to trade on the Chicago Board of Trade now?

Mr. **MAHLMANN**. Congressman, we have approximately 3,500 members.

Mr. **TALLON**. What percentage or how many of those 3,500 members are actively participating or are qualified dual traders?

Mr. **MAHLMANN**. I cannot give you an accurate number on the number of members. I can give you an estimation of preliminary results of trading volume that occurs on our exchange that is done by dual traders. As I indicated, it is preliminary, but it looks like it could be as much as 20 percent of our volume of contracts that are traded on the exchange could be done by brokers that also trade for their own account.

Mr. **TALLON**. To your knowledge, how many times has the Justice Department brought criminal penalties against any floor traders on the Chicago Board of Trade for specifically trading ahead of a customer?

Mr. **Mahlmann**. I would have to ask my general counsel because I do not know of any.

He is not aware of any, either.

Mr. **Tallon**. How would you view this legislation if criminal penalties were included in for trading ahead of a customer?

Mr. **Mahlmann**. Congressman, the exchange right now has within its rules a prohibition of trading ahead of a customer order. I think it is up to this committee if it elects to include that into the act. We have that as a rule already.

Mr. **Tallon**. Thank you. My time is up.

Mr. **English**. Ms. Long.

Ms. **Long**. Thank you, Mr. Chairman.

Mr. Mahlmann, in your testimony, you indicated that the CFTC came to the same conclusion that you came to, that the board came to at approximately the same time on July 11.

Why do you think that the board is better equipped to identify a potential emergency or real emergency and then to follow through with the execution of an emergency order—better equipped than the CFTC?

Mr. **Mahlmann**. The board and its staff are living within the market place everyday. The Board of Trade staff is monitoring all the activity of every market participant, particularly so in an expiring option. The business conduct committee is in constant contact with the office of audits and investigations of our staff, and I think their expertise—that is their livelihood—lends them a better insight or a better feeling or a better knowledge and prognostication of whether we have a potential default on our contract or not or whether we have right now a potential, very upset liquidation process in the contract.

I feel strongly that the members of the exchange that are part of that committee to monitor that, who have been delegated to do so are the best equipped to do so. They come out of the industry.

Ms. **Long**. How do you address the concern regarding objectivity that the CFTC is a more objective body than the board?

Mr. **Mahlmann**. As I indicated before, there is a requirement, every business conduct committee member has to adhere to an oath of secrecy, every business conduct committee member is asked prior to any meeting whether he has an involvement in a particular contract if that is up for discussion. He is asked to recuse himself, and I believe every business conduct committee member as well as every board member who goes through the same procedure and has to disclose whether there is a conflict of interest.

I think that is established beforehand so that you have absolute impartiality. I think it occurred in this instance. I can state for this committee that the opening question that I ask every board member when they came to the deliberation—when they were called for that meeting before the issue of the day was put before them, before any proposal was discussed, the opening question was, "Do you own or control any July bean futures?"

One party answered in the affirmative. That party was immediately recused. The rest of the board members in attendance all answered in the negative.

In addition, prior to going into the board meeting, through the office of audits and investigation, did I know, and as the only party that knew whether anybody had any July bean position as of the close of Monday night. And in addition going into the board meeting, I was the only party that knew that the CFTC was arriving at an independent decision that orderly liquidation was jeopardized before I asked the question of every board member whether they had a position or not.

Mr. NAGLE. Would the gentlelady yield?

On the question of the conflict, could I just simply ask for my own education. You indicated you inquired of the board members whether or not they had any interest, any, to quote you, "owned or controlled any positions in July soybeans," I am curious to know whether or not the members of your board would have an interest or serve on the board of any other company who had a position on July soybean futures?

Mr. MAHLMANN. The question that I asked, do you own or control, and if they answered either of those parts with no or both of those parts no——

Mr. NAGLE. Did any of the members present in the room that voted on the decision hold a position with any of the companies or brokerage houses or agencies that would have had a position of July soybean futures? I mean, for example, do you have any member serving on your board who is also a member of Cargill, the board of directors of Cargill? That type of situation? I am not saying that they do, I am just inquiring.

Mr. MAHLMANN. I said every member that was there answered in the negative when I asked him do you own or control. If you are representative of a futures commission house and you have customers potentially, he did not own or control the position of those customers that may clear through you as a futures commission house. That is not a disqualification standard.

Mr. NAGLE. That is my question. You mean I could serve on the board and make this decision and also be a member of a brokerage house who had customers that had positions that would be adversely affected or enhanced by the decision that I was going to vote on?

Mr. MAHLMANN. That is correct.

Mr. ENGLISH. The gentlelady's time has expired. The gentleman is next to be recognized, but I think we better go vote. Maybe the gentleman would like to recognize the lady in case she has another question since her time expired.

Ms. LONG. No, thank you, Mr. Chairman.

Mr. ENGLISH. Thank you very much. We will recess for this vote.

[Recess taken.]

Mr. ENGLISH. The meeting will come to order. Mr. Nagle.

Mr. NAGLE. How many members are there on the board?

Mr. MAHLMANN. Twenty-four.

Mr. NAGLE. Is Hal T. Hanson a member of the board?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. And he is the president of Cargill Co.?

Mr. MAHLMANN. He is president of Cargill Investor Services.

Mr. NAGLE. Is that a corporation or a close corporate relationship to Cargill itself?

Mr. MAHLMANN. I do not know the exact corporate relationship to Cargill.

Mr. NAGLE. Anybody there know?

Mr. GREDE. I believe it is 100 percent owned by Cargill.

Mr. NAGLE. Silas L. Hathias, Sr.—is he a member of the board?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. Let me be fair. First of all did Mr. Hanson recuse himself from the vote?

Mr. MAHLMANN. No, he did not.

Mr. NAGLE. Silas L. Hathias, Sr.—is he a member of the board?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. I have him as the director of grain operations, General Mills?

Mr. MAHLMANN. I presume that is his correct title.

Mr. NAGLE. Did he recuse himself from the board?

Mr. MAHLMANN. No, he did not.

Mr. NAGLE. It would appear to me that there were a number of people—who recused themselves?

Mr. MAHLMANN. One local trader that had 1 minute open position on a spread basis between the Mid-America Commodity Exchange and the Board of Trade. He recused himself.

Mr. NAGLE. Donald G. Andrew is a member?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. And he is the senior vice president with Shearson-Lehman and Hutton?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. John F. Benjamin, senior vice president for Drexel and Burnham?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. Gary K. Biefelt—he is with Biefelt and Co.?

Mr. MAHLMANN. Yes, he is.

Mr. NAGLE. It looks to me like people who work for Shearson-Lehman, Drexel, and Burnham, Biefelt and Co., Index Futures Corp. Group, Inc., Hollander and Ferhagen—I believe it is—Seay and Thomas, Heinweiber, General Mills, Solomon Brothers, Hager Green Co., Triple Nickel Trading Co.—all of these people's companies would have been affected if they held positions by the decision that the board took; would that be fair?

Mr. MAHLMANN. Congressman, as I indicated before, my opening question was: Do you own or control? And all of those gentlemen answered in the negative, except one as I indicated in prior testimony.

Mr. NAGLE. But you did not ask the question: Are you employed by someone who owns or controls?

Mr. MAHLMANN. No, I did not ask that question.

Mr. NAGLE. So if you go back to the question I immediately stated previously, people who made this decision were people who worked for companies, if those companies held the position in the July futures who would have been adversely affected or enhanced by the decision that the board would take?

Mr. MAHLMANN. All of those gentlemen made the statement I have no conflict of interest in deliberating the issue.

Mr. NAGLE. I will ask the question again. People who had employment with companies that if they held futures positions on the July soybeans, they would have been enhanced or diminished by the action of the board, voted on the decision that was taken by the board that day; is that not true?

Mr. MAHLMANN. No, that is not true.

Mr. NAGLE. Then I guess if you are working for Cargill, and your company does not have any—or to be precise, if you worked for a company that is 100 percent owned by Cargill—and I do not mean to pick on Cargill because I have a statement from them here I will get into—but if you work for a company that is 100 percent owned by Cargill, and Cargill could not fill its July futures position, that would not be on the Board of Trade regardless of conflict?

Mr. MAHLMANN. I do not understand the question, Congressman.

Mr. NAGLE. If you are an employer it is good to benefit by the decision you made. Would that not have been a conflict?

Mr. MAHLMANN. I think we have to go back again to the original question I asked. Do you own or control, and that was answered in the negative by each participant.

Mr. NAGLE. But you did not ask the question, are you employed by someone who owns or controls?

Mr. MAHLMANN. No, I did not ask that question.

Mr. NAGLE. Nor did you ask the question, or are you associated with an investment house whose customers own or control?

Mr. MAHLMANN. No, I did not ask that question either.

Mr. NAGLE. Tell me why working for someone who had a position would not have been a conflict to make this extraordinary decision that the board made?

Mr. MAHLMANN. If I pick on my fellow board member Don Andrew who happens to be the vice president of Shearson that you mentioned. Shearson may have customers in July beans, but he neither owns or controls any portion of those accounts and as a board member he can, because he has no conflict of interest and his customers may both be long and short and he may not know who they all are and what they have in positions. He is in a position to make by his expertise as a member of the exchange without conflict that he can make a decision.

Mr. NAGLE. The question I asked, I think, frankly, saying it is not a conflict does not define the fact that there is a troublesome aspect to the board members that made the decision on behalf of companies for which they were employed whose interest may have been impacted by the decision that they were about to render.

Who won and who lost as a result of the order?

Mr. MAHLMANN. I do not think there is one party that won; I do not think there is one party that lost. The order that was established was equal across the marketplace. It applied to both longs and shorts.

Mr. NAGLE. You would not disagree with me that Ferruzzi lost big?

Mr. MAHLMANN. I would disagree with you.

Mr. NAGLE. Please tell me why?

Mr. MAHLMANN. I would first make a statement that the whole marketplace in itself won by the exchange taking firm, independent action that there is no party by themselves that on either side of the marketplace that can be influencing the market.

Mr. NAGLE. I do not mean to quarrel, but let me refine it. Then who suffered a financial loss as a result of the board's action? Would Ferruzzi be one of those people that suffered an immediate negative financial impact as a result of that?

Mr. MAHLMANN. Congressman, we are also in a potential lawsuit that is still pending before Judge Zagle in Federal court in Chicago waiting for amendments. I cannot make a comment right now whether Ferruzzi lost money or not lost money.

Mr. NAGLE. Can you tell me whether or not Ferruzzi is suing you?

Mr. MAHLMANN. They are suing us.

Mr. NAGLE. Can I draw a fair conclusion, although you could not tell me that if they are suing you they are probably not very happy?

Mr. MAHLMANN. I presume you can draw that conclusion.

Mr. NAGLE. How much are they suing you for?

Mr. MAHLMANN. It has not been specified. They have been given a date by which time they can amend their lawsuit.

Mr. NAGLE. Could you provide for the committee a list of those individuals and organizations and business entities and corporations and brokerage houses that benefited financially by the decision of the board, and those that suffered a negative impact as a result of the decision of the board?

Mr. MAHLMANN. Congressman, I cannot provide that list to you because I cannot quantify who won and who lost.

Mr. NAGLE. The board does not have the resources or the information or the capability to generate that type of information?

Mr. MAHLMANN. Congressman, I do not have that information nor does the board.

Mr. NAGLE. Incredible.

Mr. ENGLISH. Mr. Gunderson.

Mr. GUNDERSON. Thank you, Mr. Chairman. Just one quick follow-up question in regard to Mr. Nagle's questioning. Mr. Andrew, when the question was asked whether you own or control, the answer was in the negative. Are you or is any other member of the board aware to the extent to which your company controlled when decisions like this were made?

Mr. ANDREW. I cannot speak for the other companies. I know in my own particular case, I am not privy to, in my position, I am the manager of the floor of the execution of the orders. I am not involved with the individual accounts and what their positions are, so I answered the question.

Mr. GUNDERSON. Is there some kind of confidentiality requirement at a time a decision is made and announced which prevents, what we would call lead information or inside advantage?

Mr. ANDREW. Yes, there is. I wear two hats. One is the Board of Trade hat and the other is with the Shearson-Lehman-Hutton, and they do not overlap. They are separate issues and I personally make it a point that I do not get involved into the position where I would have to compromise my position with the Board of Trade. So they are both separate.

Mr. GUNDERSON. Let me change the focus of the question a bit, because one of the issues that I think presents the greatest challenge to us in the reauthorization and the preparation for the future, especially if we do this in terms of a permanent authorization is the whole issue of international exchange or regulation. You indicate in your testimony that there has been a foreign futures exchange that now accounts for 30 percent of the total futures volume. I assume you mean volume here, or do you mean volume worldwide?

Mr. MAHLMANN. International volume.

Mr. GUNDERSON. What percent of that is American participation do you believe?

Mr. MAHLMANN. I can answer that for the Board of Trade. I cannot answer that for all exchanges. The Board of Trade domestically in the U.S. industry last year represented about 48.5 percent of the industry volume. That was after 4 years of unprecedented growth, cumulatively about 92 percent that the Board of Trade had grown over one 4-year span or the most recent 4-year span. During the same 4-year span with that kind of a growth figure, the Board of Trade's international market trade, meaning of total futures volume worldwide, declined from about 37 to 33 percent.

Mr. GUNDERSON. Can you give me your insight as to whether you believe that was a lack of particular products on your exchange or issues on your exchange as opposed to how much of that might be the result of competitive disadvantage due to regulation? Can you give me some insight on the two?

Mr. MAHLMANN. It is part of both, Congressman. As I indicated in my testimony, for instance, the U.S. Treasury debt instrument is probably the most worldwide spread held instrument substantially in Asia as well as in Europe. Europe already is trading a U.S. Treasury bond contract on the London Futures Exchange. Tokyo intends to bring it up this fall. Both ends are trying to make an end road in what used to be solely our product.

Mr. GUNDERSON. To what degree can you blame that on regulation? And if so, can you be specific as to the regulations now in effect which you believe put the American exchanges at a competitive disadvantage?

Mr. MAHLMANN. I can give you a recap of a very recent conversation with one of the governors of the Bank of England. And we talked about the legislative environment and I told him that in the foreseeable future, I would have to come before this committee to talk about dual trading, and the gentleman said, in London we call it single capacity and we used to be on that standard. But we recognize that the added capital that dual capacity can bring to a marketplace is very much wanted because it creates a better depth and liquidity in the marketplace. It creates closer bid and ask spreads, and it appears to me that we are going the opposite way than the U.S. industry is going.

Mr. GUNDERSON. Do you know of any foreign exchange that bans dual trading or regulates it?

Mr. MAHLMANN. I do not know of any. There may be some, but I do not know of any.

Mr. GUNDERSON. I guess my time is up. Thank you, Mr. Chairman.

Mr. ENGLISH. Thank you, Mr. Gunderson. I have noticed there that the chairman of the full committee has joined us, Chairman de la Garza. Mr. Chairman, do you have any comments or questions?

The CHAIRMAN. Thank you, Mr. Chairman. I will yield my time to the members of the subcommittee.

Mr. **English**. Thank you very much, Mr. Chairman. And we also have the chairman of the Wheat, Soybeans, and Feed Grains Subcommittee. He has something of interest on the soybean issue, I understand. Chairman Glickman, I would be happy to recognize you for any questions you may have?

Mr. **Glickman**. Thank you, Mr. Chairman, for allowing me to be here. I want to ask you how can a major participant in the market acquire such a large position as Ferruzzi apparently did—how do you monitor that to determine if they are in fact possessed of a legitimate hedging position. For example, I understand that the spec limits on soybeans was what?

Mr. **Mahlmann**. Three million bushels per month.

Mr. **Glickman**. Three million bushels per month and at least it was reported that Ferruzzi stated in Federal court—they had a long position equivalent to 23 million bushels of soybeans. And according to the Wall Street Journal today, this company is at war with you. I am not sure who declared war against whom, but I guess what concerns me is that how do you make a legitimate determination as to whether a company is a legitimate hedger? And do you consider a company that is at war with you a legitimate hedger on your market?

Mr. **Mahlmann**. Congressman, no comment on the war. On the other part of the question, Ferruzzi company and its affiliated companies are wholly owned companies, meaning Central Soya processing companies as one of them collectively go to the CFTC to seek an exemptive status from the speculative limits and the CFTC grants a hedge exemption to commercial market participants. And under the exemptive procedures, the CFTC approved the hedge exemptions for the Ferruzzi companies.

Mr. **Glickman**. So not only did you approve it, but CFTC approved it, right?

Mr. **Mahlmann**. Congressman, it is not in the Board of Trade's purview to approve hedge exemptions for grains. We requested that approval process on an emergency basis during the early part of June. We have it on an emergency basis for approximately another 45 days, but the approval to establish these positions was done to the best of my knowledge prior to us having this hedge exemptive procedure approval ourselves for a very short limited time, and the positions that we are talking about were approved under the Commission's hedge exemption.

Mr. **Glickman**. OK, just so I am clear because I am getting confused now. Who gave Ferruzzi a hedge exemption to go above 3 million bushels of soybeans?

Mr. **Mahlmann**. The Commission.

Mr. **Glickman**. When did they do that?

Mr. **Mahlmann**. I do not know a date.

Mr. **Glickman**. Is it monitored continuously?

Mr. **Mahlmann**. Congressman, you would have to ask the CFTC because this is hedge exemption granting which is totally delegated to the Commission. This is for grains.

Mr. **Glickman**. Let me move off of this one for a moment. In your statement you state that no trade will escape the exchange's computerized microscope. That is a quotation from your statement.

Does that mean that you will be able to determine with absolute precision who is dual trading?

Mr. MAHLMANN. It means that we are, under our surveillance microscope, auditing and reviewing 100 percent of every trade that occurs. Can we under that determine who trades for their own account and for its customer orders? Yes, we can.

Mr. GLICKMAN. Will you be able to? See the implication of your statement is that you will be able to determine with pretty much an absolute certainty who is dual trading, who is not, and then make the appropriate judgment. Is that a fair assertion?

Mr. MAHLMANN. That is a correct assertion.

Mr. GLICKMAN. At the current time, can you determine who is dual trading?

Mr. MAHLMANN. Yes, we can.

Mr. GLICKMAN. Do you know how many traders are, in fact, trading for their own accounts, as well as for customer's accounts right now?

Mr. MAHLMANN. I do not have the number, but I may be able to give you the number of our membership. No, I do not have it handy.

Mr. GLICKMAN. I think that would be useful. Let me just ask you a couple of other quick things. SWAPS, you make the point that the CFTC has basically approved SWAP trading in kind of an unregistered fashion, so you can have dual trading on SWAPS. Are you recommending that we in fact regulate SWAPS as futures?

Mr. MAHLMANN. I strongly recommend, first of all, that SWAPS be declared futures contracts. And that they fall under this committee's jurisdiction and under the jurisdiction of the Commission. So the answer is yes all the way through.

Mr. GLICKMAN. The final question goes to the number of—let me just mention one quick thing. I think the point of Mr. Nagle's question about—did any of the people who were on your board work for other companies that might have had positions—I think it refers to the fact that it was clear that a decision by the board to close out these long positions would result in a significant reduction in the market price—soybeans?

Mr. MAHLMANN. No, it was not clear. The order of the board applied to both long and short hedgers that had in excess of 3 million bushels. It therefore affected also parties that had to cover short positions.

Mr. GLICKMAN. Once a hedge exemption is granted, do you ever monitor the position of a hedger to determine how big the position gets?

Mr. MAHLMANN. We monitor positions constantly.

Mr. GLICKMAN. Thank you, Mr. Chairman.

Mr. ENGLISH. Thank you. Mr. Coleman.

Mr. COLEMAN. Let me ask a question about the spec limits that CFTC provided an exemption on in this particular case; is that correct?

Mr. MAHLMANN. That is correct.

Mr. COLEMAN. The usual limit is 3 million bushels?

Mr. MAHLMANN. That is the speculative position limit that any one speculator in the United States can hold in a single contract month.

Mr. COLEMAN. Unless they receive some sort of an exemption from the Commission?

Mr. MAHLMANN. That is correct.

Mr. COLEMAN. You know when they received this exemption?

Mr. MAHLMANN. No, I do not.

Mr. COLEMAN. Were you knowledgeable of this exemption?

Mr. MAHLMANN. Yes, we were.

Mr. COLEMAN. You were informed or you just heard about it? Did the Commission inform you?

Mr. MAHLMANN. The Commission did not formally inform us. They were permitted to carry that position.

Mr. COLEMAN. Do you think that there should be some sort of rule or requirement that you be notified of that?

Mr. MAHLMANN. Congressman, I think the Board of Trade action, as I indicated before to Congressman Glickman from Kansas, was that the Board of Trade in emergency action requested to have the jurisdiction over agricultural spec limits. We did so in early June. We got permission or our request was granted on an emergency basis and will expire roughly in 45 days. Yes, the exchange felt strongly that the exemptive procedure should also be within the hand of the exchange.

Mr. COLEMAN. I am sorry I had to step out of the room, I did not hear what you were saying.

Mr. MAHLMANN. I am sorry.

Mr. COLEMAN. I am glad you mentioned it. So the CFTC granted you some extraordinary emergency——

Mr. MAHLMANN. Only under our emergency request were we granted the exemptive procedure as an exchange, but I strongly believe we should have that power concurrently with the Commission.

Mr. COLEMAN. How common is it to receive one of these exemptions from the Commission?

Mr. MAHLMANN. Any commercial user showing justifiable reason of why they would have to exceed the speculative limits can go to the Commission and get approval.

Mr. COLEMAN. Is it not common knowledge that the amount of available soybeans was considerably less than 23 million bushels?

Mr. MAHLMANN. It stipulated in cart that the amount of deliverable supplies within the deliverable contract area attributable to the futures contract on the Board of Trade was approximately 10 to 12 million bushels which were predominantly owned by the same party that owned the futures contract.

Mr. COLEMAN. Knowing this as a fact, not as a judgment, the CFTC allowed this exemption to occur knowing that the contracts could not be fulfilled. Is this an unusual conclusion that one would draw if one knew the supply and knew the position to allow an exemption?

Mr. MAHLMANN. I think the answer would be no, because normally you would expect orderly liquidation of the contract.

Mr. COLEMAN. Let me ask a line of questions about the recusing from the discussion that the board of directors had on July 11, and ask you that if a company has a large position apparently as one did and in a market like this, is it generally known on the floor that this is occurring? Is this exemption that was granted by the Commission a matter of public record?

Mr. **Mahlmann**. It is not a matter of public record.

Mr. **Coleman**. But generally speaking, do people sense and pick up the action that there is such a position being held? Would you say this was common knowledge?

Mr. **Mahlmann**. By coffee shop talk, I would presume so.

Mr. **Coleman**. And people on the floor would definitely fall into that category?

Mr. **Mahlmann**. I would think so.

Mr. **Coleman**. So my question would be—and I am not suggesting that there is or was any wrongdoing—as we look at self-regulation and the questions that one raises with the potential conflict of interest, this was common knowledge that people could benefit one way or another having this knowledge, notwithstanding that they may have answered your question about having an interest or control on a particular date. Leading up to that date people could have, because of this common knowledge, participated in the markets in some fashion that would have benefited themselves. Is that possible?

Mr. **Mahlmann**. Congressman, I do not understand the conflict. I can make one statement. The only one, the sole member of the board, other than the president who is a nonvoting member, that knew about the proposal that may go to the board for discussion without knowing how it would come out was myself.

Mr. **Coleman**. I understand that. But it is possible that people not only on the board but other people who were traders could have—with this understanding of what was going on in the markets—obviously tried to benefit from it or reduced their exposure in the weeks leading up to a decision on July 11?

Mr. **Mahlmann**. Congressman, I cannot comment on traders that react to rumors and take positions on the rumors.

Mr. **Coleman**. Is there any reason why members of the board of directors would be in any better position to gain or to lose than any other person who was on the floor?

Mr. **Mahlmann**. No. Absolutely not.

Mr. **Coleman**. And in this particular question, since the CFTC had already made a concurrent decision, even absence the board making a decision, the effectiveness of that decision would have been the same in this particular instance. If CFTC had not taken that action then there may have been more reason to feel that a conflict of interest that one may have worked for an employer who held a position would have been more meaningful. This particular case was less so probably because the Commission had made a similar decision.

Mr. **Mahlmann**. Now the CFTC came to the same conclusion as the board, but there existed a problem in the orderly liquidation of a contract. The two entities came to that conclusion independent of each other.

Mr. **English**. Mr. Nagle.

Mr. **Nagle**. I want to go back again. Mr. Andrew, you are a senior vice president with Shearson-Lehman and Hutton, Inc.?

Mr. **Andrew**. That is correct.

Mr. **Nagle.** Was Shearson-Lehman and Hutton giving advice to customers as to whether it would be prudent or not in May and June to invest in July soybeans? Does your company give that kind of advice?

Mr. **Andrew.** I am sorry, I did not hear the question. Let me see if I hit it. Does my company give advice to buy or sell July soybeans?

Mr. **Nagle.** Yes.

Mr. **Andrew.** They give advice on the soybean market. It could be July, November or any, yes.

Mr. **Nagle.** Would the same be true for Drexel, Burnham, and Lambert? Would they render basically in the industry the same kind of advice that July futures are a good buy or July futures are a bad buy?

Mr. **Andrew.** Generically, most of the firms will have analysts in beans and they are given recommendations to buy and sell for all markets. When I say all markets, I mean all markets, not just soybeans but grains and also with soybeans, July, old crop, new crop, that type of thing.

Mr. **Nagle.** Would it be fair to say that Shearson-Lehman would have customers who would have been affected by the decision that the board took on, I believe, it was July 11?

Mr. **Andrew.** I do not know what the Shearson positions were, the customers positions were. I assume that they could have been on both sides. So I do not know, some could be winners and some could be losers.

Mr. **Nagle.** Could the same be said for Drexel, Burnham and Lambert?

Mr. **Andrew.** I really cannot speak for Drexel.

Mr. **Nagle.** The board is composed of 24 members. How many of them are independent members or public members?

Mr. **Mahlmann.** We have three nonmembers, meaning nonmembers of the exchange on our board. That is from the general public. There are three members who are members of the exchange but are members from outside of Chicago. They are nonresident members. There are eight members and members of the exchange who are currently principals or officers of Futures Commission Merchants. There are six directors whose principal occupation in life is being brokers on the exchange. And there are three members whose principal activity is to trade for their own account. In addition to that you have the president who is a nonvoting member of the board.

Mr. **Nagle.** Can you obtain and supply to the committee the open positions of all participants in the July contracts of soybeans at the end of each day from July 11, to last night?

Mr. **Mahlmann.** Congressman, under proper subpena, we will be very happy to supply the committee with the records of anybody in the marketplace on July 11.

Mr. **Nagle.** And can you obtain and supply to the committee the trades by all participants for each day from July 12 through noon today?

Mr. **Mahlmann.** Under the proper subpoena, we can supply that to the committee.

Mr. **English.** Would the gentleman yield?

Mr. **Nagle**. I would yield to the chairman.

Mr. **English**. On this particular point, it may be more proper for any requests that are made to be made through the CFTC. The law is quite clear as to the committee's right to information. And as I understand it, the CFTC then has the right and access to all the information that is in question. So as opposed to the committee going directly to an exchange, it may be more proper for us to go through the CFTC and perhaps the committee might want to get together and discuss what information—let me say this. There is already a request before the CFTC, and it is my understanding that this subcommittee will be supplied certain information. Perhaps we should review that information and determine if we need any additional information, but some of it is along the lines you are talking about, Mr. Nagle.

Mr. **Nagle**. I would like to make that a formal request of the committee, but I will defer until we have a chance to talk, Mr. Chairman. But I think probably, I would like to make a formal motion, if necessary.

Mr. **English**. Thank you very much.

Mr. **Nagle**. When Dr. Gramm was here, I am almost certain and I will have to review her testimony precisely, but I am almost certain that she told me that the CFTC did nothing when informed of the board's decision, except thank you for the information. I am just dead certain. I am quoting from a newspaper article that says——

Mr. **English**. What paper?

Mr. **Nagle**. The Journal of Commerce quotes her at the hearing as saying, as to the House Agriculture subcommittee hearing on reauthorization of the CFTC about her reaction to CBT's notice. She said, "she thanked them for the information." I thought your testimony today was as if the CFTC took an independent step or action other than just simply thanking you. Your testimony is that they—what did they do?

Mr. **Mahlmann**. Congressman, the Commission took independent action vis-a-vis one market participant by revoking the hedge exemption of that market participant, effective the close July 18 which in effect meant that that market participant had to liquidate whatever they had open, single market participant, up to and inclusive July 18, down to 3 million bushels.

Mr. **Nagle**. So if the committee were told that CFTC did nothing, that testimony would have not been consistent with your recollection?

Mr. **Mahlmann**. The CFTC took their own independent action. The Board of Trade did its own independent action. We communicated those actions to each other.

Mr. **Nagle**. With the indulgence of the Chair, you started monitoring this in May as a board?

Mr. **Mahlmann**. The July contract was started to be monitored last week of May, first week of June, after the May contract had gone off the board.

Mr. **Nagle**. Did you monitor it every day?

Mr. **Mahlmann**. On a daily basis.

Mr. **Nagle**. And the price continued to rise?

Mr. MAHLMANN. I do not recall any price movement in particular during the time from May on forward. It was irrespective of the price movement. We monitored open positions every day.

Mr. NAGLE. I guess I am curious. Would you agree that there was an upward trend in the price on July soybean futures between——

Mr. MAHLMANN. I do not recall the prices, Congressman.

Mr. NAGLE. Could you supply that to me?

Mr. MAHLMANN. Yes, we can.

Mr. NAGLE. The question I want to know is: Why did you wait so late before you finally took the action?

Mr. MAHLMANN. Congressman, you are most reluctant as an overseer of orderly markets to declare that there is an emergency. And you hope that all market participants will live within their obligation to affect orderly liquidation. Emergencies are only taken as a last resort.

Mr. NAGLE. I would characterize and I would ask you to assume for the purposes of my question. The characterization of this appears to be an attempt at marketplace manipulation by one of the market participants.

I want you to make that assumption. Do you anticipate at the CBOT that in the future you will see more of this type of market manipulation activity or to put the question neutral, more of this type of market conduct?

Mr. MAHLMANN. I cannot comment or would I even speculate whether there would be more manipulation. I cannot comment on any potential allegation of manipulation to begin with. All I can say is that the procedures in the May contract by job owning the market participants, both long and short, got us a reasonable—even though only by the skin of our teeth, orderly liquidation. That same system failed in July. Therefore, the emergency action.

Mr. NAGLE. Are we going to see more of these in the future?

Mr. MAHLMANN. That is speculative and I hope not.

Mr. NAGLE. I hope not too. In terms of the reauthorization of the CFTC, are there any steps this committee could take to see that perhaps you can act expeditiously when confronted with this situation or the CFTC can act expeditiously when confronted with this situation, assuming that it does reoccur?

Mr. MAHLMANN. We strongly hope it does not reoccur. And that the action that we took is strong enough to the participating world whether long or short, that the Board of Trade will not stand for a single party pushing the marketplace in total around.

Mr. NAGLE. You do not have to answer this today, but you are not requesting any additional tools to deal with this situation should it reoccur?

Mr. MAHLMANN. Could you repeat the question, please?

Mr. NAGLE. I am trying to get the sense of direction of how we can deal with these things in the future, if they do happen, and I share your hope that they do not. And I am asking you whether or not you think that in the process of our reauthorization, there are any additional tools that either you or the CFTC should have legislatively?

Mr. MAHLMANN. Congressman, as I indicated before, I think the exchange would like to have cojurisdiction over the exemptive process of speculative limits, but other than that, I think there are good checks and balances in place between the self-regulatory environment of the exchange and the regulatory environment of the Commission.

Mr. Nagle. Is the exchange, the Board of Trade given any consideration in light of the composition of the board and this situation specifically? Is the board given any consideration to expanding its public membership?

Mr. Mahlmann. We have given it consideration.

Mr. Nagle. That narrows it down, for or against it?

Mr. Mahlmann. I would be speculating right now as a single member of the board. But it would be my idea to expand the board by one nonpublic director. I mean, public director.

Mr. Nagle. Thank you, Mr. Chairman.

Mr. English. Thank you very much, Mr. Nagle. Mr. Holloway.

Mr. Holloway. No questions. Mr. Mahlmann, I want to thank you very much for your appearance before the subcommittee. It has been very helpful and I think that without question, the information that you provided concerning the soybean situation is most helpful as well. That is a subject of great interest and particularly this subcommittee has taken note of and I think it certainly has gotten the attention of a lot of members of this subcommittee that the question of the involvement of the CFTC. I think we were led to believe on Tuesday that the situation occurred differently than what you told us and we plan to look into that very carefully and further. So I am sure we will have an explanation from the Chairman of the CFTC. Thank you very much.

Mr. Mahlmann. Mr. Chairman, I would like to thank you for scheduling us after the expiration of July futures and I would like to thank the staff that worked diligently and has been very much available to have dialog with. Thank you very much.

Mr. English. We are looking forward to continued dialog, and as I said as we talked about earlier, as far as the legislation is concerned, I think we are talking about degrees in many areas. And we are looking forward to resolving those matter. Thank you very much.

Our next witness is James Lindau who is president of the Minneapolis Grain Exchange in Minneapolis, Minnesota. Mr. Lindau, we appreciate your coming and I know that you have been waiting very patiently and we are looking forward to your testimony. As I told our other witnesses if you would care to summarize your testimony, please feel free to do so, and without objection it will be made a part of the record.

STATEMENT OF JAMES H. LINDAU, PRESIDENT, MINNEAPOLIS GRAIN EXCHANGE

Mr. Lindau. Thank you very much, Mr. Chairman. I must say this has been an interesting day. I am James Lindau, president of the Minneapolis Grain Exchange. I am delighted to have this opportunity to talk to you. There are a lot of things that are on the table before us that are very important. I am going to try to restrict myself to a very few.

The Minneapolis Grain Exchange was established in 1881. It is an active cash grain trading center and maintains futures contracts and options on Hard Red Spring wheat and contracts only on White wheat, oats, and high fructose corn syrup.

I note that representatives from several other exchanges have already testified before this committee in connection with this year's CFTC reauthorization. Let me limit my remarks to the issues of major concern to the Minneapolis Grain Exchange.

First, a general comment. I am a newcomer in representing an exchange in a setting such as this, but I am familiar with business and government. I spent 23 years with a company that will remain unnamed, as a manager of grain trading and a feed ingredient trading business, and 11 years as mayor of the third largest city of Minnesota.

The futures industry today with all its size, strength, and variety owes much of its growth and credibility to the action of this committee in 1974. In that year you crafted legislation to create an exclusive, independent regulator to regulate the Nation's futures markets. The child of that legislation, the Commodity Futures Trading Commission, has done a good job under difficult circumstances. However, we are concerned that parts of this bill serve to revive the 1974 mandate and put micromanagement of some aspects of the industry in the Congress and out of the expert regulators. One must question whether this is either good business or good government.

Specifically, dual trading is essential to preserving liquidity in our futures markets. Dual traders are involved in every aspect of futures trading at the Minneapolis Grain Exchange. They cannot be separated from trading in the current option, or spreading against deferred options, and permit retention of any semblance of liquidity.

If dishonesty springs from dual trading, we must increase our vigilance to prevent it, even though there is no evidence of dishonest dual trading at the Minneapolis Grain Exchange. If dishonest dual trading springs from highly liquid, active futures markets, let us identify and punish the dishonest traders, but let us not, in the process, destroy the futures markets. These markets have provided the best, and often the only source of pricing information and margin protection dating back almost to the Civil War.

Technology is reaching the point that very accurate, timely audit information is available to help identify those traders who might try, unfairly, to do better than their trading skill alone might permit. At the Minneapolis Grain Exchange, we believe that our audit program provides a satisfactory means by which to verify the timing data submitted to the clearinghouse and to detect inaccurate or missing trade data on source documents.

In this regard, the Commission, during its 1988 rule enforcement review of the Minneapolis Grain Exchange, found that the exchange's 1-minute timing system was extremely accurate. The CFTC stated, "The exchange's overall accuracy rate was 96.8 percent." We believe that an accuracy rate of 90 percent or greater may be a proper target, and will, of course, continue to strive to maintain a high level of performance in this area. I will add parenthetically that our goal is certainly higher than that.

Let me take 1 minute to congratulate Mr. Cherry and his staff on their professionalism. We were visited at the Minneapolis Grain

Exchange by Mr. McDonald who was competent and thorough. It is our view that the fruits of this long, detailed investigation should be fully used by the committee as part of its responsibilities to overview the CFTC. In the main, the CFTC has more than enough statutory authority in the areas of so-called dual trading, audit trail and composition of boards at exchanges. I think it is entirely appropriate for this committee to review the record of the CFTC on these issues. It would be risky to incorporate your concern into statutory mandates.

[The prepared statement of Mr. Lindau appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Mr. Lindau. From what I know of the exchange out of Minneapolis, you do not have a single contract that would fall under the provisions of this legislation, do you?

Mr. LINDAU. That is correct, sir.

Mr. ENGLISH. So it has no impact on you whatsoever?

Mr. LINDAU. At the present time, we have no contract that would reach the limit that you have established. Obviously, we hope that that becomes a problem.

Mr. ENGLISH. But you have a long way to go?

Mr. LINDAU. I can say that with confidence. We have a long way to go.

Mr. ENGLISH. With regard to the point that you made with more than enough statutory authority. I would wholeheartedly agree with you. CFTC does have more than enough statutory authority. And one of the problems we have is that when we find an agency that is not using the authority that they are provided, we have two choices. One, we can attempt to address that problem, namely through legislation, or we can simply accept the fact that that agency chooses not to act. And in this particular case of this legislation, we have chosen to act where we see the failure of the CFTC to act. It certainly is not the desire of the members of this subcommittee or the full committee or the Congress to have to take this action. We would much prefer to sit back and say, gosh you guys are doing a great job and we are thrilled about it and go merrily on our way past the reauthorization.

That is not the case. We have some problems that we are facing. We have an investigation underway by the Justice Department that is well documented. You have just heard much of the controversy with regard to decisions that are being made. We have evident involvement by the Commission. We had Chairman Gramm come before this committee and leading this committee to believe that the CFTC was nothing more than a casual observer who received information.

We do not have much choice. If, in fact, we are going to demand higher standards. That is the real issue we are talking about is whether we are going to demand higher standards. Then we have to take that action. We are soliciting and hoping to work with the exchanges. We want to work with you, and as I mentioned, the Board of Trade and earlier this morning, the Chicago Mercantile Exchange, the New York Exchange, Kansas City, in trying to develop what those standards should be and the best way to reach those standards.

We have had the Futures Industry Association testifying that they agree with us that a carrot and stick approach is necessary if we are going to achieve those goals. That is basically what this legislation contains. It holds out a carrot, but there is also a stick. We recognize that with your audit trail and the system that you have, you are among the top exchanges in the country as far as being able to monitor and make certain that you know when any type of wrongdoing takes place, and we want to push other exchanges to reach those goals.

Mr. LINDAU. Mr. Chairman, yours is not an enviable task. I agree that it is difficult to accomplish. I think you should take some comfort and confidence in the fact that every exchange who has spoken here this morning shares your goal of creating a more honest, more reliable marketplace. So in that, we can all work together.

Mr. ENGLISH. I appreciate that very much and we are looking forward to your suggestions and your thoughts. And I am hopeful that in the next few days that we will firmly establish and detail what those standards will be. So thank you very much. Mr. Tallon.

Mr. TALLON. Thank you, Mr. Chairman. I think you told us that you do not have any contracts on your exchange that would fall into 7,000 contracts a day being traded and therefore come under certain restrictions, but with your audit trail and the technology you are using, are you able to have 100 percent audit trail that can detect any and all abuses? Can you do that?

Mr. LINDAU. Mr. Chairman and Mr. Tallon, as I indicated in my remarks, we had at the last analysis a 96.8 percent accuracy rate; 100 percent would be difficult in only one respect. We time our trading cards to the minute. If there happen to be 1, 2, or 3 trades in that same minute by the same trader, we may not be able to be 100 percent accurate, but we think that even at 96.8 percent, we are pretty close to perfect.

Mr. TALLON. And perfection is pretty difficult to achieve, is it not?

Mr. LINDAU. Of course, it is. It can only be a goal. One of the restrictive factors is the cost of getting to that point of perfection. As an exchange, we can only do what we can afford to do. We are pleased that that has got us to 96.8 percent.

Mr. TALLON. Wait 1 minute. Do you believe that if cost was no problem that you could get to an absolute 100 percent with any and all abuses?

Mr. LINDAU. Mr. Chairman and Mr. Tallon, if costs were no factor, we probably could find a person to stand by each one of our 60 or 70 traders in the pit all day and go home with them at night to make sure the trades were honest.

Mr. TALLON. From a practical standpoint, I certainly agree with the chairman that with his carrot and stick approach, but maybe his stick is too long. I do not know. Thank you.

Mr. ENGLISH. Mr. Holloway.

Mr. HOLLOWAY. We appreciate you bearing with us with the long day we have had. I am sure that you have had interest in the hearing as well as we have. I just basically say with dual trading, do you get many letters in or my perception of what America feels is that it is evil. Do you get many letters to the exchange asking you or questioning you about dual trading?

Mr. LINDAU. Mr. Chairman and Congressman Holloway, we have not had any cards or letters dealing with dual trading. As a matter of fact, the number of customer complaints that we get is very small. Ours is principally a commercial market. Dual trading has not become a household word.

Mr. HOLLOWAY. I have no further questions, Mr. Chairman.

Mr. ENGLISH. Thank you very much, Mr. Lindau. I appreciate your testimony very much.

Mr. LINDAU. Thank you for giving me the opportunity.

Mr. ENGLISH. And as I said, we will be looking forward to working with you.

Our next witness is Dr. Sanford Grossman who is with Princeton University, Princeton, New Jersey.

Dr. Grossman.

STATEMENT OF SANFORD J. GROSSMAN, PROFESSOR, DEPARTMENT OF ECONOMICS, PRINCETON UNIVERSITY

Mr. GROSSMAN. Thank you for inviting me. I am a professor of finance. I have been a professor of finance at Princeton University of Chicago, University of Pennsylvania, and Stanford University. I have worked for the Board of Governors of the Federal Reserve. My research over the last 15 or so years is involved in the study of futures and securities markets with special attention to the determinants of market liquidity and price discovery. My current research involves studying dual trading, as well as the mathematics of transactions, cost avoidance, and securities in futures markets. I have worked for the New York Stock Exchange, Katz and Bachs study of program trading. And I have recently completed the theoretical part of my study of dual trading for the Chicago Board of Trade.

I would like to if I could summarize the results of that part of the study for you. Some of this is going to sound, I am afraid overly academic, but that is where I come from.

From my point of view dual trading is said to occur when an entity sometimes trades as a broker for customers, and at other times trades for its own account. I found that dual trading is quite pervasive throughout the U.S. securities and futures markets, as well as in financial and commodity markets throughout the world. The pervasiveness of dual trading is due to the fact that many of the skills and facilities required to be a good broker are also necessary to be a good trader.

Dual trading increases the supply of both brokers and floor traders because a dual trader can earn income from two activities to cover his cost of training, his exchange seat, and time spent on the floor. He has less idle time and facilities when he can switch from the activity in low demand to the activity in high demand.

I should just mention that as a professor, this notion that you can be spending your time on two different activities and be a dual trader is very common in my business, the professor business, where we both do teaching and we do research. And there is some overlap between the skills required to be a good teacher and the skills required to be a good researcher, and when we do not spend our time teaching, we switch and do research and sometimes if you do research for too long you get a headache and you prefer to do some teaching. So this notion that your skills in trading that one has can be used for two activities is something that every research professor is familiar with.

Returning to dual trading, I found that dual trading has both a direct and indirect effect on the quality of customer services. The direct effect is an increase in the quality and quantity of brokers. The fact that dual trading increases the supply of brokers means the customer has more brokers to choose from and at a lower price. Furthermore, using a broker who is a good trader means higher quality execution for customers.

The indirect effect of dual trading derives from the increase in the liquidity of the market caused by the increase in the number of market makers. Parties who trade for their own account by buying at a low price and selling at a high price serve a market making function. Thus, the ability for an entity to use its facilities for proprietary trading results in an increased presence of market makers on the floor at times when their services are most needed. More traders standing ready to trade make for a more liquid market with smoother price changes.

In order to aid in a comparative analysis of dual trading I distinguish two types of dual trading. The first type called simultaneous dual trading occurs when a firm trades as a principal for its own account, and an agent for its customer in the same transaction. This type of dual trading is prevalent in securities markets, currency and interest rate swap markets, and the fixed income market.

As a matter of fact most member firms of the New York Stock Exchange call themselves broker-dealers. These stock exchange firms sometimes act as brokers, trading for customers as brokers, and other times trade for their house or proprietary account. Every major firm that you have ever heard of that trades stock, trades for its house account and it also trades for customers.

But it does something even more extreme than that. Sometimes it does both at the same time by taking the opposite position of a customer transaction, crossing that transaction, for example, on the floor of the New York Stock Exchange. I heard it said today that specialists are dual traders in the New York Stock Exchange, but that is an understatement. Every major firm that is a member firm of the exchange both trades for its own account and trades for customers. Simultaneous dual trading does not take place in futures markets in the sense that firms do not simultaneously take the other side or their own customers trades.

The second type of dual trading which is something that occurs in our futures markets is what I call consecutive dual trading, and this occurs when a firm trades for customers as an agent and at other times trades for its own account as a principal, but the firm does not do both in the same transaction. Consecutive dual trading occurs in futures markets, as well as in all of the markets in which there is simultaneous dual trading.

Dual trading plays a particularly important role in futures markets as contrasted with securities markets. The fact that all trading in futures takes place on the exchange floor and that spread trading is an important part of hedging strategies make the skills of a trader more necessary for a good futures broker. The immediacy required by the futures markets makes liquidity more important, and therefore makes a larger supply of market makers more critical than it would be in a securities market.

There are three types of brokerage services that I have identified that the customer needs. The first service called search involves searching for the parties who are interested in being on the other side of the trade, that is the contra-side, the contra-party to the trade. The second service called timing involves obtaining and processing information to determine how long to wait for the arrival of the most advantageous contra-party while being exposed to the risk of an adverse price move. The third service bargaining involves actively bargaining among available contra-parties to obtain the best price.

A securities broker can use his skills and sales force to prearrange trades upstairs. Upstairs search in securities markets is often an effective substitute for the downstairs working of an order where timing and bargaining skills are needed. A futures broker cannot prearrange trades upstairs. The brokerage firm cannot substitute search skills for trading skills. The order must be worked on the exchange floor. The floor broker must have the ability to trade in such a way on the floor of the exchange that he brings the other side of the trade to the floor at a good price for his customer. Therefore, floor trading skills are relatively more important in the futures market than in the securities market.

Further, much futures trading involves spreads where a customer wants to buy and sell two or more contracts simultaneously for a guaranteed net price. The customer's broker can execute the spread by trading with a local on the floor, or the broker can execute the individual legs of the spread consecutively. The latter will be in the best interest of his customer if the broker is a skilled trader, since by trading each leg himself, the broker avoids paying the local a premium for the risk in trading the spread. Such spread trading is inherently risky to a broker, since after he executes one leg of the spread his customer can hold him to a price for the other leg of the spread, which the broker may find impossible to achieve if the price moves after he does the first leg. This aspect of futures trades as well as the relatively high underlying price volatility in many futures contracts increase the trading skills burden on a futures floor broker relative to that of a securities floor broker.

Futures trading customers often have a high demand for immediacy because they are trading to hedge an underlying spot market position. The fact that immediacy of trade execution is extremely important to futures customers implies that they will have a greater demand for market makers than will be the case in markets where the cost of delayed execution is smaller. A commodity hedger bears great risk if he does not do his futures trade immediately. This risk may force him to trade using a market order, for example, to sell immediately to the highest bidder currently available. If there are few market makers, then he will receive a relatively low price, that is, his trade will have a high market impact. Thus, futures markets have a great demand for traders who in effect serve a market making function. The institution of dual trading permits this demand to be met at low cost.

Mr. ENGLISH. Dr. Grossman, we have a vote on the floor, we are going to have to make, so we will be back here just shortly. We will have to break for that vote. I am sorry.

[Recess taken.]

Mr. ENGLISH. Dr. Grossman, I am sorry about the vote. We get into these interruptions here as part of our committee process. Please continue with your statement. As I mentioned before, if you care to summarize any of your statement, please feel free to do so. It will be made part of the record.

Mr. GROSSMAN. Yes, I am just about finished. In concluding, dual trading increases the supply of the types of customer services which are relatively most demanded by futures customers. Dual trading is prevalent in the securities market, both on the floor and off the trading floor. Institutional securities trades are often prearranged off the floor, and this lessens the burden of securities floor brokers. It would be quite peculiar to eliminate dual trading for futures and maintain it for securities where the dual trading by floor brokers is less important. The elimination of dual trading from futures markets will harm customers by reducing the quality of brokers who do customer business. The best traders will trade for their own account, leaving customers with brokers who are less skilled traders.

By preventing traders from acting as brokers, the elimination of dual trading will reduce the number of floor traders and thus reduce market liquidity. Foreign markets will gain an advantage over U.S. markets causing large customers to leave U.S. markets, and these U.S. markets will therefore lose liquidity. Therefore, there are small customers who remain and they are the ones who are unable to trade overseas, will be most adversely affected by the loss of liquidity in U.S. markets. Spot markets, such as grains and the U.S. Treasury bond market will be adversely affected by the loss of liquidity in futures markets, and spot prices will become more volatile. Finally, customers will lose the freedom of choice they now have to pick either a broker who trades for his own account, or to pick a broker who trades exclusively for customers.

That is sort of the end of my formal statement. I would just like to give you one example of what goes on on the floor to make you get a feel for what the difficulty is of trading futures sometimes and why futures traders really need a skilled broker. A skilled broker is somebody who is a good trader. Sometimes you have a situation where the commodity or the spread that is to be bought, the bid is $1 and the offer is $1.10. That is a 10-percent spread. Now the customer gives his order to the broker. It could be a market order. If the broker is lazy or very risk adverse, he might just lift the offer to $1.10. Maybe if the broker is energetic and feels likes working hard and taking some risks, he might bid $1.09 or $1.05 in the hope he can get it somewhat cheaper for his customer. Now in bidding $1.05, he of course runs the risk the market will move away from him before he is ever able to get the trade done for his customer. So there is a lot of pressure on a broker about how hard to bargain and how long to wait.

A good broker has to have all the skills of a good trader to give his customer good service. I have listened to a lot of the testimony today and heard about abuses and front running and things that definitely sound terrible to me, but there is one abuse that has not been mentioned which I think economically is at least as great significance, and that is the abuse of a lazy good for nothing broker who does not act by front running adversely to you, but just does not give you a good fill. He goes in and you tell him I have a large size to buy, get me a good price. And he has a big deck; he is very busy; he has a lot of orders to do. He asks what is the market. People give him a very wide spread, as I said, the locals or whoever is there gives him a spread of $1 to $1.10 and rather than bargaining with them and arguing with them effectively and yelling and working very hard to work this order, he goes to the $1.10 and says done. And he has cost his customer perhaps 10 cents. Maybe if he had worked harder, he could have got it for $1, instead of $1.10.

There is a notion that when you give your broker an order, the broker is away from you on the floor and you cannot see how hard he is working that order creates a kind of an abuse of laziness and bad fills, which I think is very significant. And I think, institutions that encourage good traders to become brokers and dual trading is such, the institution of dual trading does encourage good traders to become good brokers and do customer business as opposed to leaving customer business, really lessens what I call the bad fill abuse.

I think in trying to regulate these markets, you should keep in mind that one of the biggest abuses in any principal agent relationship is laziness on the part of the agent and these brokers are agents and anything that can be done to increase competition among brokers by increasing the broker population through allowing dual trading is something that will give the customer a tool to deal with lazy brokers and help the customer get better fills.

That is all of my informal remarks.

[The prepared statement of Mr. Grossman appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Dr. Grossman. I appreciate that. I am not sure there is much that this subcommittee can do about legislation on laziness. That is an area we have not had a great deal of success with in the past. There has been once or twice that Congress, I think, has attempted to legislate in that area and it has not worked out well at all. It is my understanding that you have been employed by the Chicago Board of Trade to carry out comprehensive empirical study on dual trading; is that correct?

Mr. GROSSMAN. Yes.

Mr. ENGLISH. Also, it is my understanding you were employed by the Chicago Board of Trade earlier to carry out a study with regard to the proposed 1-minute time bracketing regulations and you put out this booklet; is that correct?

Mr. GROSSMAN. That looks like a reprint of an article published in the Journal of Futures Markets. It is a reprint of a scholarly journal article.

Mr. ENGLISH. Right. You were also employed by the Chicago Board of Trade to carry out that study; is that correct?

Mr. GROSSMAN. I think the study that I did for the Chicago Board of Trade led to that paper. I am not sure they commissure, but there is definitely a relationship, yes.

Mr. ENGLISH. So you were employed to do that. I noticed in this article booklet that it states, "The frequency of dual trading is itself low." And then in another point in there you state, "The frequency of dual trading are worth emphasizing or the low frequencies of dual trading are worth emphasizing." Given that fact, how can dual trading be as vital as it is, since you stated back in 1986, it rarely occurred?

Mr. GROSSMAN. I think, if I remember the context of that is that we were at that time concerned about front running abuses, and that what we did is we studied a particular time bracket. In a particular bracket, we did not find very many instances where a dual trader had both traded for a customer and traded for his own account. That does not mean that across other brackets that particular individual did not switch from becoming a trader, a broker, to a trader who is a proprietary trader.

Mr. ENGLISH. I guess the point that I am making though is that here on one hand you state back in 1986 that this is something that is a low frequency situation. It is something that does not occur that often. If that is the case, I do not understand then why it can be such a big deal this year. The other part of it is that from your testimony, you are talking about a theoretical overview. Does that mean that it has little fact and a lot of rhetoric when we talk about the question of dual trading on your study?

Mr. GROSSMAN. At the moment I have not yet done the empirical part of the study. I have finished outlining the work that needs to be done for the empirical. I do not believe there is any rhetoric here. It is an outline that is a theoretical framework used to provide a guidance as to what should be sought for in the data. Let me just emphasize again and with respect to your previous remark about the low frequency of dual trading, what we said was that the dual trading has a low frequency in a particular bracket. But a given individual who trades in a particular bracket only for himself may in another bracket trade only for customers.

The terms that we have used in the paper that you were quoting, even though that individual across two brackets had engaged in a lot of dual trading in the sense that in bracket one, he had traded only for himself, and in bracket two, he had traded only for customers, in each bracket he had traded only for himself or only for customers. So on a bracket-per-bracket basis, there was not a great incidence of dual trading, but across the whole day there may well have been a large incidence of dual trading. It is the fact that there is not a lot of dual trading within a particular bracket that lessens the occasions where front running abuses can occur.

Mr. ENGLISH. I believe you also stated in the pamphlet that a 1-minute bracketing would constitute regulatory overkill.

Mr. GROSSMAN. Is that a quote?

Mr. ENGLISH. We would be happy to give you the page number, if you would like for us to dig it up for you.

Mr. GROSSMAN. No, I do not remember. I am just asking, are you quoting?

Mr. ENGLISH. No, it is not a direct quote, but that is the context.

Mr. GROSSMAN. I think what we had done at the time was look at the costs and benefits of the proposed regulation and we had used facts to measure those costs, to estimate those costs and facts on dual trading to estimate those benefits. And we have found at that time that the facts were such that the costs seem to be higher than the benefits.

Mr. ENGLISH. And given the fact and certainly given your testimony here today, before you had done the study that you theoretically already support the concept of dual trading. You seem to have some very definite ideas before you had done the study with regard to that. And also given the fact that you have been retained by the Chicago Board of Trade which also supports dual trading, can you tell us that we are going to receive an objective study on this issue?

Mr. GROSSMAN. You should understand that I thought everybody agreed, correct me if I am wrong, that there are potential benefits to dual trading?

Mr. ENGLISH. No, that is not the question. Let me make the point. I do not want you taking off on another angle because basically what we are coming down to, on one hand you come here, you testified you are very strongly in support of dual trading. Two, you have been employed by a firm that strongly supports dual trading, and three, you are telling us you are going to do a study.

It is hard for me to understand how you could have an objective study when you have already reached the conclusion. I do not understand. I am certainly not a Ph.D. and I do not go around doing studies, but it was always my understanding whenever you conducted these studies, you are supposed to be somewhat objective and you are supposed to go and try to learn an answer, not knowing the answer before you went in and then try to prove that it is right.

Mr. GROSSMAN. Even though you are not a Ph.D., I should be articulate enough to be able to explain to you what I am doing and why I am doing it, and I hope you will allow me to do so. This study and the outline that I have given you discusses the benefits of dual trading and how you measure those benefits and where you should look for those benefits. There may well be costs to dual trading and those costs have to do with the abuses that are associated with dual trading. What I think needs to be done to come to an appropriate economic cost benefit analysis is to think of where you would look for the benefits and measure the magnitude of those benefits.

What I have set out to you is where I would look for those benefits. Now the actual numerical magnitude of those benefits are not something one is predisposed toward, they may turn out to be economically negligible. And if certain evidence arises that the abuses are not economically negligible in terms of their costs, then though I have elucidated where those benefits are, the fact that they are sufficiently small relative to the cost would mean that we should restrict dual trading.

So the mere fact that one has from a theoretical point of view said where the benefits would be sought after, does not mean that one is predisposed to the economic, numerical magnitudes of those benefits. I am certainly not so predisposed and I could not off the top of my head even give you a ballpark guess in dollars as to what the magnitude of those benefits are. I should mention to you that there are no studies of dual trading. There are no studies of the benefits of dual trading or the cost of dual trading. I think this is a completely new area and I would urge you to allow studies to go forth to measure the economic quantity of dollar values involved to get a notion of what the costs and benefits are of the quantities being regulated.

Mr. ENGLISH. I am not the one who is paying for it. You would have to talk to the folks who are paying for the study. Thank you very much, Dr. Grossman. We appreciate your testimony.

The next witness is Mr. Warren Lebeck from the National Grain Trade Council here in Washington, DC. Mr. Lebeck, we want to welcome you here today. And as we have told our other witnesses, if you would care to summarize your testimony, the written testimony will be made a part of the record.

STATEMENT OF WARREN LEBECK, ON BEHALF OF THE NATIONAL GRAIN TRADE COUNCIL

Mr. LEBECK. Thank you very much. Well, I am not even going to summarize my testimony. We have submitted a copy for the record, but after being briefed on Tuesday's hearings, I gather that you have heard several times what is in the statement and I do not think that it needs to be repeated, as long as it is in the record. But as a consequence I was advised that the committee might be better served and more interested on comments or questions that it had raised Tuesday, especially on parts of section 101, and with your permission, Mr. Chairman, and respectfully hoping only to be helpful, I would like to give some personal views based on years of observation of this business at close hand.

And I think as you know, and maybe not many people in the room know for me this is deja vu. I do not know that this is the same chair that I sat in, but it is the same place I sat in 16 years ago, and at that time there were questions about why did soybeans go to $12.90 a bushel? You have not heard any prices like that today. And why did the Board of Trade say liquidation only in July futures?

So I have been there and I might say almost reluctantly, I am here again. But just a few views of 35 years of observing futures trading. Banning dual trading at any level means that choices will have to be made and the very real fear is that the best, most competent members will either choose to trade for their own accounts or only for customers who sign releases. And I am going to get to that a little later.

It seems to me that in most instances traders would opt to trade for their own account if they had or if they wanted to have a position. I would hate under those circumstances to be a floor manager because I would have to spend every morning up until that bell rang at 9:30 finding out who is going to fill orders today and who is not going to fill orders today, and I have to wonder if that is the way to assure customers of the best possible service. If there was a monumental news item—Gorbachev deposed, a shooting war somewhere—would traders want to broker or trade and I think most of them would want to trade with monumental news and that leaves you with who is going to fill the order then.

I am talking about customer releases which is one of the things that is in your bill. A dual trading broker would be limited to filling orders only from customers who had signed releases. Some large commercials have indicated to me that they would sign releases. They already use brokers who trade and they know they can trust them. They have confidence in their floor personnel to see that their orders are filled fairly. And since this type of customer generally provides brokers with the most business, the most orders, and gives them the opportunity to trade, there would be where your best, most competent people would be, leaving smaller commercial houses with less competent brokers.

I do not believe that commission houses would sign blanket releases. I do not think their attorneys would let them. They would insist that each customer decide which type of broker he or she wants executing orders. In the view of the publicity in this proposed legislation, it would be my guess and that is all it could be obviously, most public customers would not sign releases. And thus, commission houses would have to find both types of brokers because they had both types of customers.

Referring to Commission discretion, even with the Commission given the discretion in your bill, it still would be a time-consuming affair. That is just the nature of Government and requiring reports to a congressional committee, while I understand it, I believe in it, I do not think there is any doubt it would make the CFTC extremely cautious. And this is in no way a criticism of the CFTC or of the requirement, it is just a fact that such a requirement invites bureaucratic caution, and that could be to the detriment of the market.

I know there has been a lot of talk here today, especially by the Congresswoman from Indiana, worrying about liquidity and trying to determine what is and what is not a liquid market. I do go back 16 years to the soybean market and from personal observation, Mr. Chairman, there were times when between trades there was more than 5 cents and yet there were a lot of activity in those particular markets.

The council does feel strongly about the issue of dual trading because as commercial users of futures markets, our members do not have the luxury of being able to stay out of the markets. They must be able to be buyers and sellers of futures contracts during every minute that the futures markets are open. The economic benefit of additional liquidity is difficult to measure, but it is real and cannot be refuted. Section 101 would force the unknown cost of doing without it onto the commercial users of the market. This would raise costs not only for market users, but for all who produce, use, or consume grain, in short all of us. It seems clear to the council that the cost of this supposed remedy greatly exceeds any perceived benefits.

And also it seems to me, Mr. Chairman, that we have talked about, I think, you have mentioned several times today, the stick and the carrot, there is an old saying that if you really want to get someone or something's attention that a 2 by 4 appropriately applied does the job very well. It is my feeling that the 2 by 4's that have been wielded by Tony Valukas and by this committee have done just exactly that. They have gotten the attention of the exchanges. And I think that was dramatically illustrated by the testimony here today. And it would be my hope that there can be some compromise to allow the audit trails to do the job. I think that in all cases it is better to use medicine rather than surgery. You can always keep surgery as an alternative.

The efficiency of our futures markets must be preserved and enhanced. The council urges you to keep an eye toward what greater contributions American futures markets can provide our country. This very committee continues to grapple with the issues of price risks in the production of U.S. commodities. As production decisions continue to move toward market-driven from Government-driven, the classic risk-shifting functions of futures markets will become increasingly attractive.

I do appreciate the opportunity to be here, and having had some experience with a couple of times when there was liquidation only, if there are any questions, I will do my best.

[The prepared statement of Mr. Lebeck appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you very much, Mr. Lebeck. I appreciate that. Several exchanges are part of your Council, are they not?

Mr. LEBECK. Yes, sir.

Mr. ENGLISH. So you are very familiar with that aspect of the trade. Of the involvement that you have had, you mentioned the public sector or you were talking about the public individuals, I think, trading, as opposed to grain companies and others that may be looking for various reasons to become involved. What percentage of the trade is made up of those individuals that simply may be cattlemen or a farmer or whatever that may be hedging, say in the Board of Trade? You are familiar with the Board of Trade, I know.

Mr. LEBECK. The last figure I heard on farmer participation, producer participation in the grain markets, and I have to confess, as you know I have not been that active in the last few years, was it ranged probably between 6 and 10 percent. I think that the chances are probably pretty good that that has increased but I would not think it had increased a significant amount.

Mr. ENGLISH. You think it has increased?

Mr. LEBECK. Yes, sir; I do.

Mr. ENGLISH. I was looking at the contracts that we have and particularly the big ones. For instance, now on the Board of Trade, the big contract that is being traded is not wheat or corn or soybeans even, basically the big ones are T bonds.

Mr. LEBECK. My answer was producers, meaning farmers in the agricultural markets.

Mr. ENGLISH. But we are talking about the entire business on an expanse.

Mr. LEBECK. I would have no way of answering that. That would have to come from the Chicago Board of Trade.

Mr. ENGLISH. OK, but coming with these big numbers, 295,000 contracts being traded on an average each day, as opposed to say 13,000 for wheat or 37,000 for corn, or even 44,000 for soybeans. Probably it has shrunk up considerably since the time you were talking about, has it not?

Mr. LEBECK. Are you saying that the agricultural volume is not as great?

Mr. ENGLISH. Or any individuals such as that. Whenever you have these new contracts that have come on the exchange, big contracts, huge trades taking place, high volumes of trades taking place every day. That the percentage of those individuals, if it was back during the time you were talking about, 5 or 10 percent on the agricultural contracts, if we are talking about the entire exchange itself, that has probably shrunk down would it be fair to say less than 2 percent, do you speculate?

Mr. LEBECK. If you back me into a corner, I would agree with you.

Mr. ENGLISH. I was not.

Mr. LEBECK. My figure was the number of farmers who were using the markets as opposed to how much their volume was compared to the total volume.

Mr. ENGLISH. Right. Well, I agree with that. But whenever we talk about the question of dual trading, what we are talking are mature liquid contracts. And say on the Board of Trade, T bonds are definitely mature liquid contracts, would you not agree?

Mr. LEBECK. Yes, I would agree. And I am very very happy that I happened to be president of the exchange when that contract came out.

Mr. ENGLISH. Great, and I am happy too.

Mr. LEBECK. I have just been handed a note which reminds me of something I should know better than the person who handed me the note. NFA transaction fees which apply to nonmembers of exchanges and that does not mean just individuals, but any nonmembers, range in the mid-20 percent.

Mr. ENGLISH. But that would be farms and whatever it may be.

Mr. LEBECK. It could well be pools and firms, not just individuals, yes.

Mr. ENGLISH. That does not give us a very good feel for what we are talking about. The other point that I wanted to go down to, to bring me around to that is basically what we are saying the people who are trading on the exchanges—the majority—are big companies. With regard to grains, we are talking about the big companies. We are talking about Cargill, Bunge and whoever may be wanting for whatever reason hedge or maybe even speculate the markets, correct?

Mr. LEBECK. Yes.

Mr. ENGLISH. OK, given that and you made this statement with regard to a dual trader is really trusted. They trust that broker on the floor?

Mr. LEBECK. Yes, sir.

Mr. ENGLISH. Well that is a different story than what we got from those companies. Those companies tell us, well we do not do that. We do not trust them.

Mr. LEBECK. That surprises me because the ones I have talked to, including one of the firms you named, have told me that they would sign releases for all their brokers.

Mr. ENGLISH. They would indeed. And the reason that they would is because they have their own people on the floor. They have their own people looking over the shoulder of that broker and they have their own surveillance system. In other words, they have their own built-in protection.

Mr. LEBECK. I mentioned that in my statement.

Mr. ENGLISH. But that being the case, it is not the question of whether they trust the broker, what they are doing is they are trusting their surveillance system that they personally have put in place, correct?

Mr. LEBECK. For whatever reason, they trust their broker.

Mr. ENGLISH. But whenever we are talking about these individuals, they do not have the surveillance system. They do not have somebody there to look over their shoulder. We had the gentleman here from the Minneapolis Grain Exchange. He was asked the question, could we have 100 percent perfect system. He said, yes, you stick somebody with each one of those brokers looking over his shoulder, yes, we could costwise. And that to a great extent, not totally, but to a great extent is what large companies have done and that is the reason they have built-in the protection themselves. Is that not true?

Mr. LEBECK. Yes.

Mr. ENGLISH. And then the other thing, we get down to the question of dual trading. It was said we have the gentleman who was hired by the Board of Trade, Dr. Grossman, and Dr. Grossman's account here stating, there is not that much dual trading taking place. So when we start talking about the markets moving off shore and when we start talking about the impact that this is going to have on markets, the huge impact, and then we come in and find, according to the professor who did the study back in 1986, and he is stating that the frequency of dual trading is itself low. I guess it starts kind of narrowing this thing down and makes you wonder if we may be splitting hairs on a number of these issues.

It appears to me as I mentioned earlier, if what we are really talking about here, taking away a lot of the rhetoric, we are talking about degrees. How much of the standard are we going to have? How much are we going to strengthen that standard? And I know in talking to you that you support a higher standard.

Mr. LEBECK. Absolutely.

Mr. ENGLISH. So I just want to say, I think it is important for us to go through and to bring a little bit of this out and should point out that what we are looking for is the overall public. It is the integrity of that system that I think that makes it so successful and makes it so appealing to people not only in this country, but from overseas. We just want to build just a shade more integrity into it.

Mr. LEBECK. I do not think anybody I heard today would disagree with that. I would make a couple of comments. Back in my days, I got in trouble periodically by having that attitude, sir. There have been—I know the Board of Trade and I think the Merc—both have had studies on how much of their volume is done by dual traders and the amounts that I recall just offhand run from 20 percent on up. So I realize what is great and small. I do not know what the professor—I do not understand these Ph.D's too well like you, means by great or small, but I think that the volumes do run in those ranges.

Mr. ENGLISH. I think we heard 20 percent being used today.

Mr. LEBECK. Did we not hear that today?

Mr. ENGLISH. Yes, the 20 percent was brought up. Maybe the Board of Trade ought to check with the professor in what it means by low. I think that is a good point.

Mr. Lebeck, we are going to look forward to working with you. I know we have already talked about some of these areas and we feel that you all can help us a great deal, and given the experience that you have had. And I know that you are very interested in seeing stronger standards. We are going to be looking forward to working with you.

Mr. **Lebeck**. As you are, and I thank you.

Mr. **English**. I appreciate your testimony. Thank you very much.

Mr. Jontz, we have a panel up next. I am going to let you lead off by introducing one of our witnesses, if you would, one of your constituents?

Mr. **Jontz**. Thank you very much, Mr. Chairman. I am delighted to have the opportunity to do that. Mr. Chairman, I know you have conducted very extensive hearings today and earlier this week, and you have heard from the president of the exchanges, and you have heard from academics, and you have heard from a lot of different perspectives.

I am glad to welcome a constituent from my district who represents a very important perspective to all of us and that is the local country elevator and farmer. I think it is important that we hear from them too. So I am delighted to introduce to you John Fredrickson who is a partner in Kentland Elevator and Supply in Kentland and Newton County in my district. I have represented Newton County in one capacity or another for 15 years, and I know that Mr. Fredrickson brings to us today a very important perspective, and I believe the other witnesses on this panel do also.

I want to conclude my comments, Mr. Chairman, by thanking you again for the tremendous effort you have put into these hearings, and even though I am no longer a member of your subcommittee, I am going to be following your lead very closely and I know that you have done a very thorough and comprehensive job with these hearings. And I thank you very much for allowing me to sit in this afternoon for just a little bit of the testimony.

Mr. **English**. Delighted to have you back and feel free to come by any time. It is always a pleasure to have you with us, and Mr. Fredrickson, the very high recommendation that you got and I want to introduce our other witnesses who have equally high credentials. Mr. Dave Danker who is from Perryville, Missouri. I believe, Mr. Coleman, I am not sure you are from his district are you?

Mr. **Danker**. Congressman Emerson's.

Mr. **English**. Congressman Emerson's district, OK. And we have Mr. Joseph Kane, who is floor broker with the Chicago Board of Trade. Mr. Kane, we are happy to have you here today, and Mr. Ralph Weems, who is a former president, American Soybean Association from West Point, Mississippi. Mr. Weems, we are happy to have you, and Mr. Fredrickson, we will let you start off our testimony. And as we have told our other witnesses, if you would care to summarize your testimony, your written testimony will be made a part of the record.

STATEMENT OF JOHN L. FREDRICKSON, PARTNER, KENTLAND ELEVATOR AND SUPPLY, INC.

Mr. FREDRICKSON. Thank you, Chairman English and also thank you Congressman Jontz for the introduction. As Congressman Jontz introduced me, I am a partner in Kentland Elevator and Supply, a country elevator located in Northwest, Indiana. I have been involved in the management of grain elevators for over 20 years, and involved in the ownership of this present facility for the past 11 years. I also own and operate a small farm, serve as an officer of our State grain and feed association, and serve as director of an insurance company.

The firm I represent is an independently owned elevator with three locations. The primary business of our country elevator is purchasing grain from area farmers and reselling it to grain processors, grain exporters, livestock, and poultry feeders.

When we purchase grain from a farmer, we are at risk in the marketplace until we have sold the grain. We may choose to sell the grain through a user for immediate delivery, or we may choose to keep the grain in one of our storage facilities to sell at a later time. If we choose to store the grain, we must transfer the market risk to someone else immediately. This is accomplished by hedging the grain in the futures market at the Chicago Board of Trade. We place an order to sell futures contracts for the amount of grain we have purchased. When we decide it is no longer economically feasible to hold the grain, the futures portion of this transaction is offset by buying futures contracts at the same time the cash grain is sold. Our elevator's margin is the selling basis, less the buying basis.

The execution of the futures orders is a critical component of the transaction. It must be completed at the best possible price and executed very promptly. The liquidity and flexibility provided by dual traders who can trade for their own account as well as execute customer orders, is a contributing factor for our country elevator to provide the best price at the lowest cost.

Sometimes we may determine that it is not economic to sell the cash grain as the futures expiration approaches and decide to roll the hedge forward to a deferred contract month. This transaction is called a spread, since it involves the simultaneous purchase and sale of futures contracts in different months. Successful execution of a spread trade is obtained by utilizing an experienced dual trader who can leg into the position by executing one side of the trade when futures prices for that contract are more favorable. He may not be able to obtain the desired price from the other leg of the spread, but may place it in his own account at possibly a slight loss in order to satisfy the customer and keep his business. The ability of the dual trader to obtain favorable prices for spread trades helps increase the liquidity in relatively less deferred contract months, and results in more accurate indications to market participants of the cost of carrying commodities.

The banning of dual trading could increase transaction costs for our elevator by widening bids and offers due to less pit participation. This increased cost will cause either a reduction in our return on investment, or most importantly a reduction in prices paid to farmers by our firm.

Dual trading increases the supply of both brokers and floor traders because a dual trader can earn income from two sources to cover cost of training, an exchange seat, and time spent on the floor. Dual trading encourages greater competition between brokers, thus keeping commission costs down. If dual trading is banned, the best brokers will trade for their own account, decreasing the number of brokers available to execute orders for our elevator. This will reduce the liquidity of the marketplace, thus making it more difficult to have our orders executed promptly at the market.

Dual trading is voluntary on the part of customers; customers can now prohibit their brokers from dual trading if they choose. Additionally, U.S. futures exchanges are engaged in a continuing process of improving their market surveillance systems. If abuses can be curbed through adequate surveillance, there is no reason to eliminate the practice like dual trading which contributes to the liquidity for which American markets are known.

Simply stated the ideal legislation would preserve dual trading while ensuring the exchanges bear the responsibilities for detecting its possible abuse. I strongly urge Congress to evaluate the pros and cons of dual trading before making a final decision on this vital issue. Your decision will effect the entire agricultural industry, as well as the future of our markets.

[The prepared statement of Mr. Fredrickson appears at the conclusion of the hearing.]

Mr. **English**. Thank you, Mr. Fredrickson. Mr. Danker.

STATEMENT OF DAVE DANKER, VICE PRESIDENT AND GENERAL MANAGER, BUCHHEIT GRAIN, INC.

Mr. **Danker**. Chairman English and members of the committee, my name is Dave Danker, and I am the vice president and general manager of Buchheit Grain, Inc., located in Perryville, Missouri. Buchheit Grain is a small, family owned feed, grain, and general merchandise business founded in 1934.

My purpose in coming here to speak to you today is to attempt to explain how we use the futures markets, in particularly the spread market to effectively manage our business, and how that relates to one of the subjects your committee is reviewing, that is, dual trading. We have approximately 1,250,000 bushels of space in two different locations. In order to survive as a grain merchant, we must fill all of our space at harvest and hopefully handle 60 to 70 percent of that volume once again after harvest.

In order to manage this need in a business-like manner, it is imperative that we prespread our space and the volume of grain that we hope to handle post-harvest. A brief example of prespreading would be a simultaneous purchasing of 10,000 bushels of December corn futures while selling 10,000 of March corn futures. As the corn is purchased from farmers during October, we would simply sell the December corn futures. This would automatically spread the purchase out to the March futures position.

Prespreading is an inexact science, but as one gains experience, it becomes easier to establish reasonable goals and achieve them. We like to enter our spread orders prior to the time the contract actually trades. Oftentimes this results in getting a good fill that may never be available at any other time during the marketing cycle. Quite often, due to poor liquidity in those distant contract months, our broker has to leg a spread in order to have it filled. By legging the spread, the broker first takes one side of the spread, then fills the other side as soon as he is able.

During the time elapsed between the execution of both legs of the spread, the broker assumes the risk of not getting the spread filled at or above my order. If he fails to accomplish that fill and ends up trading the spread at a lesser amount, the loss is for his account. The broker's ability to dual trade gives him an opportunity to offset these losses by trading for his own account throughout the day. I feel that this will make spread brokers more willing to take chances in order to get their customers the best possible fill, thereby maintaining their reputation and position in the marketplace.

I had a personal experience with this situation last winter that I would like to share with you. Last January, I began planting for the 1989-1990 marketing year. I budgeted the purchase of 200,000 bushels of soybeans at harvest. And I estimated that we could buy at harvest, store, and later resell soybean, if we could get our November/March spreads set at 17 cents per bushel or better. I called my trading firm and entered a broker to spread 200 November/March soybeans at 17 cents or better. A few days after the March contract first came on the board, my spread got filled at 19 cents. Given what I know about spread conditions at that time, I have to assume that the trade was legged.

And I realize that not all trades have such a happy ending, but I believe it illustrates my point that if you trade through a brokerage firm that does the job in policing and controlling the trading activities of the brokers that it uses, you can get good honest fills. It seems to me that if one is knowledgeable about the current conditions of the market, offers spreads, options and some futures transactions at a given level or better, he will obtain the fill he wants.

The key to obtaining these fills is in prior evaluation of the quality of broker that you choose to deal with and in the existence of surveillance systems that detect and deter abuse. The issue is not whether the broker dual trades. The real issue is whether or not there are adequate monitoring systems in place to detect cases where the practice of dual trading is abused.

In summary, I would like to stress that I feel the current system of allowing brokers to both fill orders and take risks for their own account, provides a more liquid market, and most probably a more aggressive trader. The system, as it exists, has provided us with the structure to build a successful small business. I would like to encourage you to provide a means for protecting and improving the integrity of the current system of dual trading rather than changing something that, in my mind, already works. Thank you.

[The prepared statement of Mr. Danker appears at the conclusion of the hearing.]

Mr. ENGLISH. Thank you, Mr. Danker. Mr. Weems.

STATEMENT OF RALPH WEEMS, FARMER, FORMER PRESIDENT, AMERICAN SOYBEAN ASSOCIATION

Mr. WEEMS. Thank you, Mr. Chairman and Mr. Coleman and members of this subcommittee. I am a farmer from West Point, Mississippi. I believe I am the only farmer we have had here today. But I have been involved with soybeans for 30 years. I have been associated with the Mississippi Soybean Association for 22 of those years, and I worked my way up to the presidency of the American Soybean Association in 1984. I should briefly depart from this and say that the views that I am expressing today are mine and not necessarily those of ASA.

I became associated with the CBOT through the agricultural advisory committee in 1984. I was elected chairman of that ag advisory committee in 1985 and the chairmanship of that committee carried with it a 3-year term on the board of directors as a public director, a seat that I held until February 1988.

While I was at the Chicago Board of Trade as an outside director, several cases came before the board at that time, one which I vividly remember and would like to call to your attention at this time. It had to do with a trader who was suspected of outside—not outside trading—but front running and this was naturally very interesting to me as a farmer to see how a fellow director would approach this thing with me as an outsider on their group. But, sir, it was my opinion and I hold that opinion to this day, that those gentlemen took that hearing to the deepest part of their heart and that they did their dead level best to do what was supposed to be done at that particular time.

The board's decision on that case was explosion. I said then and I repeat now, that I wish every farmer in America could have been there that day and seen what happened. Because I think it would increase the confidence in our market system enormously. I have, as I stated, had tremendous confidence in the board and I still have that confidence today. Thank you, sir.

Mr. ENGLISH. Thank you Mr. Weems. Mr. Kane.

STATEMENT OF JOSEPH J. KANE, FLOOR BROKER, CHICAGO BOARD OF TRADE

Mr. KANE. Chairman English, Mr. Coleman, and Mr. Jontz, first I would like to thank you very much. Ralph said he thinks he was the only farmer here. I know I am the only floor broker trader here. My name is Joseph Kane. I am a member of the Chicago Trade since 1952. I have also been a member of numerous other exchanges, including Chicago Mercantile Exchange and the New York Coffee and Sugar Exchange. For 7 years, I was the director of the Chicago Board of Trade and served on most of the major committees of the exchange, including the business conduct and the floor governor's committee. In fact, in 1968, I was the chairman of the reorganization committee of the exchange that was responsible for introducing public members to our board of directors, also out of town directors to our board of directors, and creating the floor governor's committee which has the primary responsibility for policing the conduct of our members on the exchange floor.

I was born, raised, and educated in Chicago and I am the father of eight children. Many of my children have worked in one capacity or another in the futures business. I have been at the Board of Trade so long that I can say that I knew the grandfathers of two of our present directors. I say this for a reason and I hope it will become apparent.

I know the Board of Trade's rules, customs, and practices. I have seen those rules, customs, and practices evolve. I have also seen the competition for business which exists on the floor and the solid ethical standards which are upheld by most members combined as a potent force for the protection of the customer.

Nevertheless, I know that this subcommittee is concerned about the practice of dual trading. I believe I am in a good position to discuss this practice and the results which govern this practice because throughout my 37 years as a floor broker, I have also routinely traded for my own account. Over the years, I have given a lot of thought to dual trading. In 1975, I was coauthor of a study on that topic which formed part of the report of the chairman of the advisory committee on the regulation of contract markets and self-regulatory associations of which I was a member. As you remember, when the CFTC was formed, there were four groups formed to aid from the industry. I was privileged to be a member of one of those groups.

In that report, we came to the conclusion that dual trading was a major ingredient in the liquidity of our markets and that its elimination would impair that liquidity without conferring any measurable benefits on the public. We recommended that dual trading be preserved, but that rules be adopted which clearly prohibit a broker from buying or selling for his own account while holding orders for others at the market price at the same time. We also recommended that surveillance systems be improved, so that the exchanges in conjunction with the CFTC could ensure that abuses of that and other practices were detected and punished.

I believe our recommendations were valid then and that the last 14 years have vividly demonstrated their validity. In the intervening years, our markets have enjoyed unprecedented growth in volume and liquidity, making them the envy of the world. At the same time, the Chicago Board of Trade and other exchanges have adopted straightforward rules to make the misuse of dual trading, that is, trading ahead of the customer order, a trade practice violation.

And most important of all, over the last 10 years, and in particular the last 5 years, the exchanges have taken strides unimaginable in 1975 to create and implement effective surveillance systems for detecting all trading abuses, including trading ahead. In particular, the computerized audit trail codesigned by the Chicago Board of Trade and the Chicago Mercantile Exchange has demonstrated a detection and deterrence capability offered by no other financial markets in the world. At least that was the view expressed by Nicholas Brady as head of the Presidential task force which studied the 1987 stock market crash which was alluded to by Mr. Melamed this morning in his testimony.

I do not pretend to speak for the entire floor broker community, but I know if I conducted a survey of the many many responsible floor brokers whom I work with each day or whom I know around the various exchanges in the country, they would want to stress for you the following points. First, they would like to tell you that you would take away a major means of servicing their customers if you take away the dual trading privilege from the broker, as in the manner that it was just outlined to you. Dual trading allows the floor broker to go after the best fill for his customer, knowing the broker has the flexibility, if necessary, to trade out of resultant losing positions through his personal account whenever the opportunity arises.

Second, they would tell you they support the adoption of the best, most comprehensive surveillance system devisable as a means of protecting themselves as well as their customers. That is an important point that a good surveillance system protects the broker, as well as the customer.

The message I would leave with you is simple. We have the best most liquid markets in the world. I am not an economist, but I believe the rational review of the economic literature available on the subject will lead to the conclusion that dual trading has contributed to the unrivaled success of our markets. In copying every aspect of our market formula in an effort to win business from us, foreign markets have also copied us in permitting dual trading. The foreign markets do not have our surveillance capability. They do not have the know-how and they do not have the commitment to eliminate trading abuses and the perception that abuses exist. Let us use our know-how and our commitment to keep U.S. markets in their preeminent position. With your help, we can preserve our liquidity, and all of the factors that contribute to it, including dual trading, while reinforcing the integrity for which we must be equally well known.

As a little adjunct, I would like to say that I think that I have showed you that for more than 20 years, our goals have been the same. I do not speak for anyone but myself, but like the exchanges, my goal has been to try to be of help in this instance, and I hope that I have been of some help today.

[The prepared statement of Mr. Kane appears at the conclusion of the hearing.]

Mr. **English**. Thank you very much. I appreciate that, Mr. Kane. One thing that I guess puzzles me a little bit, Mr. Kane, is this particular legislation we are looking at has a provision in it that says, anyone—any of these three gentlemen—who does not care whether their broker is involved in dual trading or not, all they have to do is sign a paper saying, I recognize my broker is involved in dual trading. It is fine with me, give him my blessing. Approve him. That is it.

We have had testimony today—I mentioned Dr. Grossman, but we will go back to the earlier testimony—that some 20 percent of the trades may have dual trading involved. So we are talking about any contract, any particular contract that we are talking about, and let us assume that we go with the 20 percent. Then we fit into the question that any customer who so wishes or does not care whether his broker is involved in dual trading signs off for it.

We have also heard that the majority of the business on any contract is going to be firms, grain companies, and so on and so forth, and they have their own people looking over their shoulder. I guess after you fit all of that together, it is hard for me to understand, how this is going to have that kind of major impact on any contract, I do not care what it is. Because if in fact you gentlemen are representative and you do not care or you support dual trading, everybody signs off. Though there is no impact, is there? Is that not true, Mr. Kane?

Mr. **Kane**. I think that you have one segment of an industry here that would sign off perhaps on this situation, but I think Mr. Lebeck brought up an important point in his earlier testimony. Although the commodity head of a particular futures commission merchant may be perfectly willing to sign off or to solicit his customers' opinions, I am not sure that their legal department—and I am not an attorney—would allow that to happen.

Mr. **English**. Let me point out though, the model that we are following comes from the Chicago Mercantile Exchange. That is where it comes from. That is where that provision comes from. Their lawyer does not seem to have a problem with it. He does not seem to have any difficulty with it. The thing that I wonder about, we were talking earlier about with Mr. Lebeck, the Chicago Board of Trade today may have less than 2 percent—I am probably being too generous, maybe even less than 1 percent, maybe even less than one-half of 1 percent—of their trade represented by gentlemen like we have here, whether it be farmers or whatever, a very very small percentage.

We have then the contracts, the trading that is taking place on these contracts are by firms, big firms. If they do not have any problem with dual trading, fine with me. They sign off. They have their own people there. They run their own business. So I do not understand where all these people are going to be driven away from this market because we have the provision that says that folks that do not want their particular broker involved in dual trading have a right to say so, and—our right to refuse to give that approval.

How much business are we going to lose because of that, Mr. Kane? How much business would you lose? How many of your customers that you have, do you feel would not sign that paper for you?

Mr. **Kane**. I do not have any idea how many would or would not sign because I have a business that is both commercial and retail business. And the retail business would be in jeopardy because of what I brought up before. And I think that would be the important aspect personally that I would look at in that regard. It would force me to make a decision.

Mr. **English**. What kind of decision are you going to have to make?

Mr. **Kane**. I would have to make a decision whether or not I would remain a broker or whether I would become a trader.

Mr. **English**. Why?

Mr. **Kane**. Because if 50 percent or more of my income were to be displaced——

Mr. **English**. If you have all of these customers out there and it seems to me, everything I have heard of you, Mr. Kane, you are a very reputable person, one who has an excellent reputation. I am sure that over the years you have built up an awful lot of satisfied customers. Do you think that just simply because, hey, folks, customers, I am involved in dual trading. Most of them already know it, do they not?

Mr. **Kane**. Yes.

Mr. **English**. And if they know that, how many of them do you think——

Mr. **Kane**. I jumped to a conclusion. May I define a customer in my mind?

Mr. **English**. Sure.

Mr. **Kane**. A customer in my mind has a twofold aspect. A customer in my mind may be a futures commission merchant and then the ultimate customer would be the customer of the futures commission merchant. The relative retail customer of that futures commission merchant would not know necessarily who this order is going to. He would judge it on the basis of the futures commission merchant. That is where the difference——

Mr. **English**. It is his money. Should he not have the right to make that decision?

Mr. **Kane**. Oh, yes. He has that right—right now.

Mr. **English**. How does he have that right? He can tell that commission merchant, I do not want anybody that is involved in the dual trading carrying out my order, and how does he find out for sure that that is done?

Mr. **Kane**. I do not know how he finds out.

Mr. **English**. That is the problem we are into. The thing that comes down. As I said, here we are talking about 20 percent of the business. And then we are talking about narrowing that on down—the lack of confidence that I sense in the industry about getting customers to sign that paper is frankly surprising. I felt that most brokers, most people in industry would be very confident that the customers are satisfied, the customers are happy. You gentlemen here seem very satisfied with the arrangements that you have with whoever your brokers are. You seem to me to be the kind of gentlemen that would sign that paper. Would not you three? Any one of you who would not sign it?

Mr. **Danker**. Yes, I would, sir, and I think our degree of satisfaction has come over years of education and experience with a particular broker, and our confidence is built up probably more so in the futures commission merchant.

Mr. **English**. So you do not know who your broker is, do you?

Mr. **Danker**. I do not know, but we have the ability to watch our trades as they are entered and see how they are filled.

Mr. **English**. How do you do that?

Mr. **Danker**. We have up to the second quotations on our screen.

Mr. **English**. But you do not know whether this guy that is out there—you do not know who this broker is? You do not know what he is doing?

Mr. **Danker**. No.

Mr. **English**. So if he in fact traded ahead of you and he was not picked up on the audit trail, you would never know it would you?

MAY 19,1989

Representative Dan Glickman, Chairman
House Agriculture Committee
Subcommittee on Wheat, Feed Grains and Soybeans

Dear Chairman Glickman:

I am writing to call to attention to the disaster of the 1989 wheat crop in our area. I planted 2000 acres of wheat for harvest of which now I have 150 acres left. The 150 acres of wheat that I have left will be used solely for seed wheat and will not provide a means of income whatsoever.

This disaster could be very well be the final blow to many farmers that have struggle through the last several years of low commodity prices and high expenses. We need you and your committee to consider this disaster and well as the past several years of hardship that the American farmer has been faced with and act swiftly.

We need immediate assistance for now and a long term, low interest loan for the future. The emergency disaster loan program that is currently available is a farce.

Thank you for your time and I greatly appreciate you and your committee for taking the time to listen.

Sincerely Yours,

Larry Don Smith

Larry Don Smith
Rt.1 Box 32a
Perryton, Tx 79070

Texas Agricultural Extension Service

The Texas A&M University System
Lipscomb County Extension Service
P.O. Box 127
Lipscomb, TX 79056
(806) 862-4601

May 17, 1989

Memo To: U.S. Congress & House of Representatives, Agriculture Committee, House Sub Committee on Wheat Soybeans and Feed Grains

Subject: Disaster Relief

The disaster relief is an important step in helping farmers and ranchers survive this critical time in production agriculture. Not only do farmers need help, but so do the cattlemen. I would like to address the hay situation for Lipscomb County Texas producers.

There are approximately 49,000 acres of Lipscomb County land under the Conservation Reserve Program which could be used for haying. The hay carryover is normally 20,000 tons per year. Listed is the carryover for the last few year: 1986-87, 11,000 tons; 1987-88, 0 tons; 1988-89, 5,000 tons estimated. The 1986, 1987, 1988 carryover reduction was due to severe winters, however the increase from 0 to 5,000 tons for 1988-89 was due to an abnormally mild winter. Yet the carryover is less than ¼ of normal because of the drought of 1988. This 5,000 ton carryover could be less as some producers have had to continue feeding hay.

98% of the Conservation Reserve Program grass in Lipscomb County is Old World Bluestem. Varieties include WW Spar, Caucasian, Ganada and Plains. If the CRP acres could be harvested for hay this could greatly reduce the added burden of producers with CRP grass from having to buy hay. In addition it would reduce the price other producers have to pay for hay.

If approved early enough CRP grass could be cut at the time when protein is high and tonnage good. However, a delay could reduce the nutritional value and palatability of this hay.

Listed below are the averages of Old World Bluestem production:

	Harvest Date	Lbs/Acre	% Protein
1st cutting	June 15	2000	11%
2nd cutting	September 1	3000	9%
1st cutting	July 15	3500	8%
1st cutting	Plant Maturity		6%

From the above illustration it can be seen that the later this grass is cut the more protein value of the grass decreases. If no further rain is received the early cutting would produce high quality hay for cattlemen.

This issue is one that should be looked at carefully.

Sincerely,

Herbert Sprague Jr.

Herbert Sprague, Jr.
County Extension Agent-Agriculture

HS:jm

Spurlock Farms
HCR 1, Box 256
Stratford, TX 79084

House Agriculture Committee
Wheat, Soybean & Feed Grains Subcommittee
Chairman: Dan Glickman

Dear Mr. Chairman and Members of the Committee:

My father and I farm 3,700 acres in Sherman County in the Texas Panhandle. We have 1,500 acres of wheat base, irrigated and dryland, of which our average yield is 50 bushels per acre . Due to adverse weather conditions, freezing and drought, our 1989 harvestable wheat crop is 230 acres which may yield 15 bushels to be used for next year's seed. The balance of the acres has been destroyed.

We would like for you to act favorably to a Disaster Program which would include wheat damaged by freeze.

Respectfully,

Neal Spurlock

Wesley Spurlock
Neal Spurlock

ROCKY
MOUNTAIN
FARMERS
UNION

COLORADO NEW MEXICO & WYOMING

P O BOX 39628 • 4605 PARIS STREET • DENVER COLO 80239 • PHONE (303) 371-9090

Testimony of

VICTOR STOUT, Board Member
Rocky Mountain Farmers Union

Before the House Agriculture's Subcommittee on

Wheat, Feedgrains, and Soybeans

Texas A & M Research and Extension Center
Friday, May 19, 1989
Amarillo, Texas

ROCKY MOUNTAIN FARMERS UNION
COLORADO, NEW MEXICO & WYOMING
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Testimony of

VICTOR STOUT, Board Member
Rocky Mountain Farmers Union

Before the House Agriculture's Subcommittee
Wheat, Feedgrains, and Soybeans

Good morning, Mr. Chairman. My name is Victor Stout, and I farm near Clovis, New Mexico. My farm extends to just one mile from the panhandle of Texas, so the conditions I am about to describe include the west edge of the Texas Panhandle.

I farm wheat and milo and run cattle in the northern part of Curry County. I was born and raised in this area, and I have taught vocational agriculture, as well as farmed. I serve on the board of Rocky Mountain Farmers Union.

The drought of 1989 has been devastating to my area of eastern New Mexico. Dryland wheat is 90 percent gone, either plowed up or will not be carried to harvest, in other words, abandoned. Except for a few isolated spots where there have been small showers, there is nowhere where there is moisture to plant milo. The native grass pastures look like the dead of winter.

Some of the irrigated wheat has been abandoned, and what remains will have such poor yields that it will lose money. This is due to freezes as well as dry weather. Irrigated corn and milo have been planted, but they already have such a big water bill against them that they will probably not be profitable.

Very few cattle remain in the area. Since there is little pasture, most have either been sold or moved to areas where there are better pastures.

Rocky Mountain Farmers Union is a general family farm and ranch organization representing about 18,000 farm and ranch families in New Mexico, Colorado, and Wyoming. I serve on the board of this organization and represent the membership in New Mexico on this board. At a board meeting held in Denver recently, I heard of conditions in southeastern Colorado, and the drought has affected that area as badly.

We in Rocky Mountain Farmers Union are pleased that the Secretary of Agriculture is concerned about the drought and has announced some programs to help alleviate the effects of the drought. However, many of the provisions of the Secretary's program will be of only marginal assistance to the farmers in these areas. We believe the effects of this drought are deeper and more serious than the Secretary realizes.

Farmers in our area have been under economic stresses from forces beyond their control for several years now. Many have not been able to keep up with the furious economic treadmill we have been on. Some have only been able to survive by loan write-downs and other forms of economic assistance. The recent Farm Credit Act has helped to save them from financial ruin. This drought threatens to negate the beneficial effects of the Farm Credit Act.

Assistance to the farmers in this drought must be far reaching and immediate. The magnitude of the drought calls for more comprehensive assistance than the Secretary's plan provides. We suggest the reauthorization of the Disaster Assistance Act of 1988, the act that was instituted to help the drought-stricken farmers of the Midwest last summer. This measure should be amended to address the particular problems of the farmers of this area, but there is no need to reinvent the wheel. The legislation worked last time and will work again to help relieve the pressures of the drought here in eastern New Mexico and west Texas.

We urge you to take strong and immediate action to aid the farmers and ranchers of this area. As you have heard, the conditions here are genuinely disastrous, and unless assistance is swift and generous, we may lose many of the family farmers and ranchers in eastern New Mexico and west Texas.

I thank you for the concern you have shown by coming here today and for your patience and understanding in receiving this testimony. All of us here appreciate your efforts. I would be glad to try to answer any questions you might have.

Ochiltree County Farm Bureau
109 South Main
Perryton, Texas 79070

May 18, 1989

Representative Dan Glickman, Chairman
House Agriculture Committee
Subcommittee on Wheat, Feed Grains & Soybeans

Dear Chairman Glickman:

I am writing to call to your attention the grave consequences facing farmers in this area as a result of the several disasters which have thus far befallen the 1989 wheat crop.

The most severe damage has been of course due to the fact that we have received no appreciable rainfall since last September. The effect of this drought has been further compounded by a hard freeze in February and an abnormal infestation of of insects which preyed on the already stressed wheat with devastating results to irrigated as well as to dryland crops.

I believe that I am speaking for all farmers in the Texas panhandle in requesting that wheat producers in this area, as well as those elsewhere, be afforded the same concern and consideration shown corn belt producers during the drought of 1988. A similar disaster relief program would appear to be fair and equitable to all.

We would greatly apreciate any and all efforts by you and your committee on our behalf, as we face a true disaster which may result in a genuine death blow to the already stressed economy of agriculture in this area.

Sincerely,
Larry Swink
Larry Swink
Rt. 1 Box 58
Perryton, Texas 79070

May 16, 1989

Representative Dan Glickman, Chairman
House Agriculture Committee
Subcommittee on Wheat, Feed Grains & Soybeans

Dear Chairman Glickman:

I am writing to call to your attention the grave consequences facing farmers in this area as a result of the several disasters which have thus far befallen the 1989 wheat crop.

The most severe damage has been of course due to the fact that we have received no appreciable rainfall since last September. The effect of this drought has been further compounded by a hard freeze in February and an abnormal infestation of insects which preyed on the already stressed wheat with devastating results to irrigated as well as to dryland crops.

In my own case, which I think is representative of that of the average wheat grower in this area, I planted 800 acres of dryland wheat and will be fortunate to cut 100 acres. If I did not have need of seed wheat from this acreage, I would have destroyed it along with the other 700 acres. It will by no means provide me with cash income in any amount. I have further destroyed one-third of my irrigated crop, and will count myself lucky if the remaining two-thirds of this acreage produces even one-half its normal yield. In combination, I have effectively lost approximately 85% of my normally marketable crop. It is my considered opinion that this is a reasonably average figure for all producers in this area, although there are a number who will harvest no wheat whatsoever.

I believe that I am speaking for all farmers in the Texas Panhandle in requesting that wheat producers in this area, as well as those elsewhere, be afforded the same concern and consideration shown corn belt producers during the drought of 1988. A similar disaster relief program would appear to be fair and equitable to all.

We would greatly appreciate any and all efforts by you and your committee on our behalf, as we face a true disaster which may result in a genuine death blow to the already stressed economy of agriculture in this area.

Sincerely,

Joe E. Thompson

Joe E. Thompson

Box 215
Farnsworth, Texas 79033

5-17-89

To Whom It May Concern:

My name is Gwen Turner. I farm 480 acres in Ochiltree County, Texas.

I will not cut any wheat this year due to no moisture thru fall and winter.

A disaster payment will let me plant next fall.

I will appreciate your help in getting our County and others a disaster program.

Thank you,

Gwen L. Turner
905 Kentucky
Perryton, Tx 79070

5-18-89

Dear Sirs:

Due to the severe drought I will cut little or no wheat on the 480 acres I own in Ochiltree County, Texas.

I am retired and depend on the income from this farm for my livelyhood.

A disaster payment will enable me to plant next fall.

Thank you,

Jean Black Williams

P.O. Box 827
Perryton, TX 79070

I'm Kenneth Wooster

I farm 2200 acres of Ochiltree farm ground about 6 miles N.W. of Perryton.

I had 1700 acres dry land wheat + about 91 irrigated. All was gone by the 1st of February - most of it died because of dry + unseasonably warm weather. Because the ground was so dry + loose it made it very hard to control the bugs.

Since May 16th we have had about 11 inches of rain which has now caused Problems the other way.

Because of high water we had to move all the sheep + horses. Now we will have to pay rent to keep the livestock. We have some ACR acres that would handle the sheep but of course we can't graze it.

Also I own 1/2 of Panhandle Implement Co. — We have real problems there when the farmers have a disaster.

We are trying to continue to give the farmer good service but we are having to keep all expense to a minimam.

This thing would be impossible if we couldn't turn the pressure over to God.

We hope you will consider some sort of disaster program. — The family farm + farm equipment business depends upon it

Thanks for your consideration

Kenneth Worth

STATEMENT FROM ROBERT YOUNG
DALLAM COUNTY TEXAS
MAY 19 1989

CONGRESSMAN DAN GLICKMAN:

Gentlemen my name is Robert Young. I am a farmer and rancher in Dallam County, Texas and Texas County, Oklahoma. I am President of Dallam county Farm Bureau with a membership of 590 family farmers and ranchers in Dallam County Texas.

Dallam County has 157.000 acres of Hard Red Winter wheat. There are 78,500 dryland acres that rely 100% on snow and rain fall. Since September of 1988 we have received less than 1 inch of rain. With a very dry and warm winter the wheat never had a chance to go dormant, thus it used up all of the moisture the ground had stored from the previous year. In late January and early Febuary the temperature went from the high 80's to -10 degrees in 3 days, freezing the wheat plant and killing it. According to county ASCS we have a 98% loss in the dry land wheat. The 76.900 acres of wheat lost from drought and freeze amounts to 1.615.000 Bushel of wheat at today's market this amounts to $6,500,00.00 loss to the panhandle area. The loss from the inputs on 76,900 acres at $20.00 is equal to $1,538,000 giving a total loss of $8,038,000.00 to Dallam County for dry land wheat. Due to the freeze we lost 50% of the irrigated wheat 39,000 acres, 1,950,000 Bushel worth $7,800,000.00. With input losses of $150.00 per acre or $5.850,000.00. This amounts to a loss to Dallam County irrigated farmers of $13,650,000.00 A total loss on all wheat irrigated and dryland of $21,688,000.00. This does not include any loss of livestock pasture. With the lack of sub moisture it is very unlikely that we will be able to raise a dry land milo crop.

We pray that after you gentlemen look at all the information brought before you that you would consider extending the 1988 FARM PROGRAM into 1989 and include freeze damage.

As you can see some of the farmers and ranchers are going to be out of business this year and a lot of people ~~wold~~ will be without jobs causing a lot of unemployment in Dallam County.

I personally farm 2600 acres of dryland wheat and 1800 acres of dryland milo and have disastered 100% of the wheat and doubt if we well have enough moisture to raise any milo as I do not have any sub moisture.

One of our Farm Bureau members planted 2300 acres of irrigated winter wheat. He well be able to harvest only 120 acre because of the freeze.

ROBERT YOUNG
RT 1 BOX 110
DALHART .TEXAS 79022

REVIEW OF DROUGHT CONDITIONS AFFECTING KANSAS AGRICULTURE

SATURDAY, MAY 20, 1989

House of Representatives,
Subcommittee on Wheat, Soybeans, and Feed Grains,
Committee on Agriculture,
Great Bend, KS.

The subcommittee met, pursuant to notice, at 8:30 a.m., in the Fine Arts Auditorium of Barton County Community College, Great Bend, KS, Hon. Dan Glickman (chairman of the subcommittee) presiding.

Present: Representative Roberts.

Also present: Representative Slattery.

Staff present: Greg Frazier and Anne Keys.

OPENING STATEMENT OF HON. DAN GLICKMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. **Glickman**. Good morning and welcome to today's hearing of the Subcommittee on Wheat, Soybeans, and Feed Grains of the House Agriculture Committee. We had the hearing today to prove that when this subcommittee goes out to hold a drought hearing we bring rain. [Laughter.]

I am delighted to be here with my colleague Pat Roberts who is a member of the subcommittee. We are in his congressional district, and our colleague Jim Slattery from the Second Congressional District who is a member of the House Budget Committee which decides dollar spending for agriculture.

I know we have invited all members of the Kansas delegation, House and Senate. They are here presenting statements for the most part, and all of their statements will be included in the record.

I am going to have a brief opening statement and then turn it over to Mr. Roberts and Mr. Slattery.

This is the second day of hearings the subcommittee has had on the 1989 drought, the Disaster Assistance Program, and in addition talking to some degree about 1990 farm programs, because they will relate to what we are talking about today.

We had a hearing in Texas yesterday, in Amarillo. The chairman of the full committee, his name is Congressman E (Kika) de la Garza, was there. He is sorry that he could not be with us today, but he figured that we could take care of it. The only thing I can tell you is after the hearing yesterday, where we had a crowd about the size we do today, I am confident that the chairman is going to schedule a markup of the disaster assistance bill and move it quickly through the House Agriculture Committee. So that is good news, and one that will provide some help and some assistance, and hopefully we can get that process started soon, next week, or if not next week right after we come back after the Memorial Day break.

The hearing today, in terms of what Pat and I and the members of the committee are interested in, is pushing disaster legislation. We will do our best and I am confident that it will happen.

The hearing today will focus on some things that will make our job easier in writing legislation. One, of course, is we want to hear about the extent and cause of damage to the winter wheat crop and to other crops and to the livestock industry as well. We want to hear weather conditions. I frankly, am very upset with the U.S. Department of Agriculture meteorologist. I do not think that producers and ranchers and the public of this country have been well served by weather forecasts that tend to be very related to what the policymakers at USDA want those weather forecasts to be.

I just think it is incumbent upon us to get a true, honest accounting of the weather, both this year as well as in future years, and we will get some of that information today.

Another question will be is the extent to whatever we do, applies to winter wheat or 1988 crop only, or is a general extension of the disaster program to apply to spring crops as well. I hope we can get some testimony on that. In Texas, yesterday, we heard from the Grain Sorghum Association who strongly believe that the legislation ought to include both because, in south Texas, they believe they will not be able to get their grain sorghum crops planted at all and I would be interested in your views on that.

The issue of crop insurance and how it relates to what we are talking about today. Obviously there has been extraordinarily small participation and therefore a disaster program is needed. But the disaster program is not going to be a miracle. The amount of disaster assistance if we take last year's bill is not going to compensate people fully, or even near fully, for their losses. And the problem will be worse this year because the target prices fall under the 1985 farm bill. So the relief under the disaster program this year is not even going to be as large as it was last year if we just extend the program. So I think we have to look at the crop insurance program to see some personal examples of how it works, or does not work, to provide some assistance to producers during disaster time. I know one of our witnesses today is a member of the National Crop Insurance Commission and he will also testify on those points as well.

I mentioned at the beginning that while this hearing is disaster related, I think that you all who will testify should not be afraid to talk a little bit about the 1990 farm bill and changes in that law that might help deal with weather- or drought-related problems. Yesterday Congressman Slattery and I were in Kingman County and we looked at two fields of wheat. One was destroyed and one was OK, approximately 25 bushel per acre yield, and the field that had fairly good wheat was a field that oats had been planted on before or had late silage, we are not exactly sure what, but in any event the whole issue of a farm bill that allows greater substitution might in fact give greater protection from drought damage, and I know that both Pat and Jim have been interested in that question as well.

The other thing I think we ought to think about today, too, is that the Department of Agriculture is projecting big surpluses of wheat, a reasonable carryover of wheat, notwithstanding this drought. I think we need to ask people who are in the grain and feed business, the elevator business, is the carryover, is the surplus as big as what the Department of Agriculture would say it is at this time.

A couple of personal observations and I will introduce my colleagues. If the disaster is as broad in scope and the damage as big as I think it is, the loss of this State will be profound. If it is even 125 to 150 million bushel loss, the direct loss to the Kansas economy is $500 to $600 million. When you leverage those dollars out, it will have monumental consequences to the entire State. I am sure the Governor will talk about that, and also to the areas of the State which are affected which tends to be a swath that runs southwest to northeast, the main part of it through the center part of Kansas.

As I said, the multiplier is great, the small community effect is gigantic, the effect on the credit system of this country is tremendous. It will reverse some gains made in the last year on agriculture, and the personal loss and grief to producers will be just overwhelming.

Yesterday a Texas banker testified that in the panhandle, 10 percent of their borrowers would not make it unless there were some disaster assistance, and 25 percent would be on the edge.

In any event, we are here to learn. This is a hearing that is going to produce some results. It gives you an opportunity to come to us and tell us what is on your mind and what you think we ought to be doing to deal with some of these problems.

Now I would be glad to turn the mike over to my colleague, Pat Roberts. We are delighted to be in the big first, real Kansas.

OPENING STATEMENT OF HON. PAT ROBERTS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. ROBERTS. First of all I want to welcome you to the big first or what I call real Kansas. It certainly has to be—is unreal it just means, well you know what I mean. [Laughter.]

I want to first associate myself with your remarks, Mr. Chairman. And more especially in regard to the weather forecasters, we had a hearing in Washington 2 days ago and Dr. Strohman, who does a good job, indicated at that particular time that the wheat crop in Kansas was suffering about a 30-percent loss, maybe 37 percent. That is not true. If you go to the historical proportions of what we usually produce, that is, 480 bushels and we produce more per acre than any other State, it is about a 50-percent loss; a 60-percent loss. That is the bottom line.

What are you holding, a drought hearing in the rain? It sounds a little strange or a little unique or a little bizarre, but the fact remains that we have lost the winter wheat crop to the tune of 50 or 60 percent and we need a disaster bill.

I will be more than happy to peer over your shoulder, Mr. Chairman, in regard to the weather forecasting policy of the USDA. We used to have a fellow out in Dodge City who is now stationed out in Colorado who still gives the weather forecast out in Goodland, Leonard Bowman. Maybe we need to put Leonard Bowman in USDA.

I would like to introduce at this time Mrs. Betty Joe Roberts and Mr. Robert Weinieger.

Mrs. Roberts is here representing Senator Nancy Landon Kassebaum; and Mr. Weinieger is here representing Senator Bob Dole and I would ask permission, Mr. Chairman, to insert both of the Senators' statements in the record at this point.

[The prepared statements of Senator Nancy London Kassebaum and Senator Robert Dole follow:]

Statement for the House Subcommittee on Wheat, Soybeans, and Feed Grains
by Senator Nancy Landon Kassebaum
May 18, 1989

I thank the Chairman of the Subcommittee on Wheat, Soybeans, and Feed Grains for scheduling this hearing to consider relief measures for farmers who have been seriously affected by extremely hot and dry weather conditions. Many of us realize the magnitude of the damage to the wheat crop and pastures, but it is most important to hear recommendations and proposals from those here in Kansas who have been personally affected.

Earlier this week, I joined with Senators Bob Dole and David Boren in introducing legislation to extend last year's Drought Assistance Act to losses for crops planted in 1988 for harvest in 1989. This would allow farmers with up to a 35 percent loss to keep deficiency payments previously advanced. If the disaster is greater than 35 percent, 65 percent of the target price will be made. On any disaster in excess of 75 percent of program yield, disaster payments will equal 90 percent of the target price.

Although much of the attention has been on the wheat crop, livestock producers also are affected by this year's drought conditions. Dry pastures have prompted farmers in Kansas, Oklahoma, and Texas to sell an unusually large number of cattle to feedlots. This has caused the futures prices to decline steadily in the past thirty days. Those with foundation cow herds in Kansas cannot find pastures with adequate cover, and the cash market is off as much as $200 per head.

The drought relief legislation, which we have proposed, will make available up to $25 million to provide livestock transportation assistance. While this assistance to transport livestock was included in the 1988 Drought Assistance Act, the Agriculture Secretary was allowed to implement the program at his discretion. Consequently, this program was not available to producers. Our bill would mandate this assistance to transport livestock during the livestock emergency.

Another key provision in our legislation would direct the Soil Conservation Service to provide 50 percent cost-share assistance with terracing, ponds, and other practices for management of limited water supplies. The Agriculture Department would provide not less than $25 million for these water development projects.

The situation is serious, and I believe we must move expeditiously to address it, particularly since there are offsetting savings in the budget to fund this assistance.

The Agriculture Department estimates that our legislation would result in payments between $250 million and $350 million for the 1989 wheat crop. Department officials also agree that with the average market price for wheat continuing to increase, there will be more than enough savings from current programs to pay for extended relief.

Reflecting changes in wheat supplies, market prices continue to rise and this is reducing government exposure. The administration had assumed $1 billion in deficiency payments to wheat farmers participating in the 1989 program. This was based on $3.60 per bushel as the season average market price. New estimates of the average price will be closer to $4.10, which would mean very little or none of that $1 billion would be spent.

The legislation which I have sponsored is primarily directed at winter wheat producers and those with livestock operations. However, a provision does extend the authority for the Farmers Home Administration to make guaranteed loans to qualifying rural businesses which have suffered losses due to the drought.

Mr. Chairman, I also want to point out that federal crop insurance still has major problems and is not effectively addressing these kinds of situations. Last year Congress recognized this fact and established a commission to ensure a thorough review of the Federal Crop Insurance Corporation. These recommendations for improvements will be submitted to Congress this July. I believe it is vital that we then take steps to improve crop insurance programs.

In the interim, I believe it is essential that we pass legislation to open the way for extended disaster assistance for farmers now facing a disaster as serious as the one that struck other parts of the farm belt last year. I urge committees in both the House and Senate to act promptly.

DROUGHT AID FOR FARMERS

STATEMENT BY SENATOR BOB DOLE

MR. CHAIRMAN, I APPRECIATE YOUR SUBCOMMITTEE HOLDING HEARINGS IN TEXAS AND KANSAS ON THE DROUGHT. THIS WILL HELP UNDERSCORE THE SEVERITY OF THIS YEAR'S DROUGHT ON CROP AND LIVESTOCK PRODUCERS.

AN EARLY LOOK

SECRETARY YEUTTER CAME TO KANSAS TO SURVEY THE DAMAGE IN MID-APRIL AND CONDITIONS HAVE DETERIORATED SINCE THEN. THE SECRETARY DID USE HIS DISCRETIONARY POWERS TO PROVIDE SOME ASSISTANCE SUCH AS HAYING AND GRAZING DURING THE PRINCIPAL GROWING MONTHS AND ACCESS TO LIVESTOCK FEEDING PROGRAMS, BUT THE CONDITIONS HAVE GOTTEN SO BAD THAT FEDERAL AID WILL BE THE KEY TO THE SURVIVAL OF MANY FARMERS.

PASTURES AND SET-ASIDE ACRES HAVE HAD ONLY SPARSE GROWTH IN MANY AREAS, INDICATING THAT HAYING AND GRAZING ON SET-ASIDE ACRES MAY BE OF LITTLE BENEFIT. CONCERN OVER ACCESS TO ADEQUATE FORAGE AND WATER SUPPLIES FOR COW HERDS HAVE CAUSED HEAVY RUNS OF CATTLE TO FEEDLOTS AND MARKETS. OBVIOUSLY, THE LONG-TERM FINANCIAL IMPACT ON CROP AND LIVESTOCK PRODUCERS WILL BE SEVERE, WITH SOME OBSERVERS ESTIMATING OVER $800 MILLION IN LOSSES. NOT ONLY FARMERS, BUT RURAL BUSINESSES WILL BE HURT DUE TO REDUCED SPENDING ON BASIC GOODS, EQUIPMENT AND SUPPLIES.

I HAVE ASKED USDA TO ALLOW HAYING AND GRAZING ON CONSERVATION RESERVE PROGRAM (CRP) ACRES AND I UNDERSTAND THIS OPTION IS UNDER CONSIDERATION. PRECAUTIONS SHOULD BE TAKEN TO ENHANCE WILDLIFE AND PROTECT ESTABLISHED GRASS STANDS IF THIS OPTION IS APPROVED.

MOST RECENT CROP STATISTICS

AS OF MONDAY, 85 PERCENT OF THE STATE'S WHEAT CROP WAS RATED IN THE POOR-TO-VERY POOR CATEGORIES. TOPSOIL MOISTURE WAS RATED 99% SHORT AND SUBSOIL MOISTURE WAS RATED 100% SHORT. OUR PROJECTED WHEAT CROP OF 202 MILLION BUSHELS WILL BE ONLY ONE-HALF OF ITS POTENTIAL. ALTHOUGH WE HAVE RECEIVED RAIN IN RECENT DAYS, IT IS TOO LITTLE, TOO LATE FOR MANY FARMERS.

SENATE RESOLUTION

CLEARLY, OUR FARMERS NEED HELP SOON. RECENTLY, THE SENATE UNANIMOUSLY APPROVED A RESOLUTION INTRODUCED BY SENATOR KASSEBAUM AND I, AND OTHER WINTER WHEAT STATE SENATORS, URGING CONGRESS TO ACT IN A TIMELY MANNER TO PROVIDE DISASTER PAYMENTS TO WINTER WHEAT FARMERS THROUGH AN EXTENSION OF THE 1988 DISASTER ACT.

DISASTER ASSISTANCE ACT OF 1989

ON THURSDAY, SENATOR KASSEBAUM AND I ALONG WITH SENATORS BOREN, NICKLES, BENTSEN, GRAMM, BAUCUS, BURNS, PRESSLER, WIRTH, PRYOR, DASCHLE AND DOMENICI INTRODUCED BIPARTISAN LEGISLATION TO EXTEND THE 1988 DISASTER ASSISTANCE ACT TO CROPS PLANTED IN 1988 FOR HARVEST IN 1989.

LAST YEAR CONGRESS PASSED A MAJOR DISASTER ASSISTANCE BILL FOR PRODUCERS WHOSE CROPS WERE DAMAGED BY ONE OF THE WORST DROUGHTS IN THE PAST HALF CENTURY. THE DISASTER ASSISTANCE ACT OF 1988 RECEIVED BROAD BIPARTISAN SUPPORT. WE WERE ABLE TO HELP FARMERS WITHOUT ADDING TO THE FEDERAL BUDGET DEFICIT BECAUSE WE WERE ABLE TO USE SAVINGS RESULTING FROM LOWER DEFICIENCY PAYMENTS AND HIGHER MARKET PRICES.

UNDOUBTEDLY, LAST YEAR'S BILL SAVED MANY FAMILY FARMERS IN THE CORN BELT AND NORTHERN STATES, WHERE THE DROUGHT WAS MOST SEVERE. WE FELT PRETTY FORTUNATE IN KANSAS LAST YEAR UNTIL FARMERS TRIED TO PLANT THEIR WHEAT CROP LAST FALL. THE EXTREME DRY CONDITIONS BEGAN TO SET IN LATE IN THE YEAR AND HAVE PERSISTED THROUGH THE WINTER AND SPRING MONTHS.

BASIC LEGISLATIVE PROVISIONS

I HAVE ATTACHED A TITLE SUMMARY OF OUR BILL TO MY STATEMENT FOR INCLUSION IN THE HEARING RECORD. OUR BILL IS SIMPLE AND STRAIGHT-FORWARD. WE WOULD EXTEND THE 1988 ACT TO CROPS PLANTED IN 1988 BUT HARVESTED IN 1989, WHICH WOULD BE MOSTLY WINTER WHEAT, THE CROP IN THE MOST SERIOUS TROUBLE. THE PROVISIONS WOULD BE ADMINISTERED UNDER SIMILAR TERMS AND CONDITIONS AS LAST YEAR WITH RESPECT TO PAYMENT RATES, BENEFITS, REQUIREMENTS ON FEDERAL CROP INSURANCE PARTICIPATION IN FUTURE YEARS AND SO FORTH.

CURRENTLY, ONE OPTION OF PRODUCERS WHO, DUE TO FAILED WHEAT ACRES, REPORT LESS THAN 92% OF THEIR PERMITTED ACRES, IS TO HAVE THAT PORTION OF THEIR ACREAGE ELIGIBLE FOR "0-92" BENEFITS. OUR BILL INTENDS TO GIVE THESE PRODUCERS AN ADDITIONAL OPTION -- TO RECEIVE DISASTER BENEFITS IN LIEU OF 0-92 BENEFITS BASED ON THEIR INITIAL SEEDED ACRES UP TO THE PERMITTED WHEAT ACREAGE FOR THE FARM.

IN ADDITION, OUR BILL WOULD REQUIRE THE SECRETARY TO PROVIDE COST-SHARE FUNDS, ON A LIMITED BASIS, FOR TRANSPORTATION OF LIVESTOCK TO AREAS WHERE FEED AND WATER EXIST. WE WOULD ALSO PROVIDE LIMITED COST-SHARE FUNDING TO LIVESTOCK PRODUCERS WHO HAVE HAD TO IMPLEMENT EMERGENCY WATER PROJECTS, SUCH AS REVAMPING OLD WELLS OR INSTALLING PIPELINES TO BRING SCARCE WATER TO THIRSTY LIVESTOCK.

WE HAVE ALSO AMENDED THE $200 MILLION LOAN GUARANTEE PROGRAM, ESTABLISHED IN LAST YEAR'S LEGISLATION, FOR SMALL BUSINESSES IMPACTED BY THE DROUGHT. OUR BILL WOULD ALLOW BOTH PRINCIPAL AND INTEREST TO BE GUARANTEED UP TO 90%, MAKING THE PROGRAM MUCH MORE WORKABLE FOR SMALL BANKS AND BUSINESSES. THIS WILL BE AN IMPORTANT MEASURE BECAUSE THE FULL RAMIFICATIONS OF THE DROUGHT ARE JUST NOW BEGINNING TO BE FELT ON MAINSTREET AMERICA AND COULD PERSIST FOR YEARS TO COME.

THE BILL WOULD EXTEND FOR ONE YEAR THE 1985 FARM BILL PROVISION ALLOWING PRODUCERS TO PLANT UP TO 20% OF PERMITTED ACRES TO SPECIFIC NON-PROGRAM CROPS WITHOUT LOSING BASE. CROPS ELIGIBLE INCLUDE CANOLA (EXCLUDING SOYBEANS), OTHER VARIETIES OF RAPESEED, SUNFLOWERS, SAFFLOWER, FLAXSEED, KENAF, CRAMBE, GUAYULE, MILKWEED AND MEADOWFOAM .

THIS PROVISION WILL "BRIDGE THE GAP" BETWEEN THE 1989 AND 1990 CROP YEAR SINCE THE AUTHORITY UNDER CURRENT LAW EXPIRES WITH THE 1989 CROP YEAR. CROPS SUCH AS CANOLA, A FALL-SEEDED FOOD-OIL VARIETY OF RAPESEED, IS A GOOD ROTATION CROP THROUGHOUT THE GREAT PLAINS AREA AND OTHER FARM STATES. THIS AUTHORITY SHOULD BE EXTENDED BEFORE THE AUGUST RECESS SO THAT PRODUCERS CAN MAKE PLANTING DECISIONS.

THE PROVISION EXPANDS THE LIST OF CROPS NOW SPECIFIED IN THE FARM BILL TO INCLUDE CERTAIN INDUSTRIAL CROPS. EARLIER THIS YEAR I WAS PLEASED TO BE A GUEST SPEAKER AT THE FOUR STATE REGIONAL CONFERENCE ON NON-FOOD USES HELD IN KANSAS CITY. THIS CONFERENCE CLEARLY HIGHLIGHTED THE NEED FOR GREATER FLEXIBILITY TO BUILD THE PRODUCTIVE CAPACITY OF CROPS FOR NON-FOOD USES SUCH AS INDUSTRIAL LUBRICANTS AND NYLON FIBERS AND MANY OTHER PURPOSES.

WHEN WE WERE PREPARING OUR SENATE RESOLUTION, WE ASKED USDA TO ESTIMATE THE COST OF EXTENDING THE DISASTER ACT TO SPRING CROPS. USDA INDICATED ONLY ABOUT ONE-QUARTER OF THE SPRING WHEAT AND CORN CROPS HAD BEEN PLANTED AT THAT TIME AND COST ESTIMATES WERE NOT AVAILABLE. THERE ARE SOME IN BOTH THE HOUSE AND SENATE WHO WANT A WIDE-OPEN BILL, ONE THAT APPLIES TO ALL CROPS. IT WOULD SEEM BEST NOT TO JEOPARDIZE OR DELAY HELP TO WINTER WHEAT FARMERS NOW BY WAITING ON THE OUTCOME OF CROPS JUST PLANTED WHOSE HARVEST PROSPECTS ARE MONTHS AWAY FROM BEING KNOWN.

BUDGETARY ASPECTS

THE MAY 4TH LETTER FROM USDA, WHICH WE INSERTED INTO THE CONGRESSIONAL RECORD WHEN THE SENATE PASSED OUR DROUGHT RESOLUTION, NOTED THAT THE PRESIDENT'S JANUARY BASELINE ESTIMATED DEFICIENCY PAYMENT OUTLAYS WOULD BE $1 BILLION FOR WHEAT PRODUCERS AND THAT IT APPEARED WE WOULD HAVE ENOUGH SAVINGS FROM THE DECLINE IN DEFICIENCY PAYMENTS AS A RESULT OF RISING PRICES TO OFFSET THE COST, WHICH USDA ESTIMATED TO BE UPWARDS OF $350 MILLION, DEPENDING ON THE SEVERITY OF LOSSES AND EXTENT OF FURTHER DETERIORATION.

IT APPEARS THAT THE CONGRESSIONAL BUDGET OFFICE (CBO) SHARES THE VIEW -- THAT THERE WILL BE A SUFFICIENT OFFSET IN FY 1990 BASED ON CURRENT CROP CONDITIONS FOR WHEAT -- IN THEIR PRELIMINARY ANALYSIS. OUR BILL SPECIFIES THAT FUNDS WOULD BE MADE AVAILABLE FROM THE DIFFERENCE BETWEEN THE LEVEL OF DEFICIENCY PAYMENTS ESTIMATED IN THE JANUARY BASELINE AND THE MOST RELIABLE ESTIMATES BASED ON THE CURRENT CROP CONDITIONS FOR WHEAT.

HOWEVER, AS USDA INDICATED, THE NEXT OFFICIAL RE-ESTIMATE OF CCC OUTLAYS, TO BE RELEASED IN THE MID-SESSION REVIEW THIS SUMMER, WILL INCLUDE THE REDUCTIONS IN DEFICIENCY PAYMENTS DUE TO THE DROUGHT. THAT MEANS WE MAY NEED TO ACT QUICKLY IF WE ARE GOING TO BE ABLE TO COUNT THESE SAVINGS.

CROP INSURANCE

I WOULD ALSO REITERATE SECRETARY YEUTTER'S COMMENTS THAT THE MOST RELIABLE LONG-TERM APPROACH IS CROP INSURANCE. OBVIOUSLY, CONGRESS WILL NOT ALWAYS HAVE THE OPTION TO PASS DISASTER BILLS DURING TIMES OF EXTREME BUDGET CONSTRAINTS. THE FEDERAL CROP INSURANCE COMMISSION WHICH CONGRESS AUTHORIZED LAST FALL HAS MADE PRELIMINARY RECOMMENDATIONS WITH A FINAL REPORT DUE LATER THIS YEAR.

HOPEFULLY, CONSTRUCTIVE CHANGES CAN BE MADE TO ATTRACT GREATER PARTICIPATION, IMPROVE ADMINISTRATIVE FUNCTIONS AND MAKE THE PROGRAM ACTUARIALLY SOUND.

I WOULD HOPE WE DON'T PURSUE OPTIONS THAT WILL CREATE EXCESSIVE LOSSES TO THE FCIC. ALTHOUGH EXTENDING SIGN-UP FOR SPRING PLANTED CROPS MAY HAVE BEEN A WORKABLE IDEA EARLIER THIS SPRING, WE ARE APPROACHING THE POINT WHERE TO DO SO NOW WOULD ONLY RESULT IN "BUYING LOSSES" WITHOUT ANY SIGNIFICANT REVENUE BEING GENERATED.

EXTENDING LAST YEAR'S PROVISION REQUIRING PRODUCERS WHO RECEIVE DISASTER PAYMENTS AND HAVE SIGNIFICANT LOSSES TO SIGN UP IN FUTURE YEARS SEEMS THE SOUNDEST WAY TO ORIENT PRODUCERS TO THINK ABOUT THIS RISK AVERSION OPTION. WE ALSO NEED TO CONSIDER THE IMPACT THAT MANDATED SIGN-UP FOR FCIC WOULD HAVE ON COMPETING COMPANIES THAT SELL HAIL INSURANCE.

CONCLUSION

ONCE AGAIN, MR. CHAIRMAN, I APPRECIATE THE SUBCOMMITTEE'S HEARINGS TODAY AND YESTERDAY AND I HOPE WE CAN MOVE QUICKLY FORWARD ON A LEGISLATIVE SOLUTION IN TIME TO USE THE BUDGET SAVINGS, AS MENTIONED EARLIER, AND PROVIDE A HELPING HAND TO WINTER WHEAT FARMERS AND CATTLEMEN.

Mr. ROBERTS. Nancy's statement pretty well sums up the bill that has been introduced in the Senate and has dramatically improved the chances of disaster legislation. That statement simply goes over the need for the legislation and the facts and figures that the Governor will be talking about, and that bill includes, it is a very simple bill. It simply says that any crop that was planted in 1988 should be covered by the drought assistance. It also mandates some assistance in regard to transportation assistance to the hard pressed livestock producer. And it also has in there some cost sharing for some—development in regard to the livestock producer.

Mr. Chairman, I cannot sit here and look out in the audience and see so many friends and partners in government without saying one thing. You mentioned the grief that could result in terms of the pain and the trauma that you witnessed down in Texas. I am so proud of these producers and these ranchers and farmers who have taken of their time to come here today, having come through a decade of trial and tribulation and then having been at the place where we had just about made it with 2 good years, not the best years by any means, but 2 good years, and just at the time when we are going to come back we get hit by this drought. And I am so proud of these people in relation to how they supported the drought assistance to corn country last year despite the fact that we had all sorts of other problems, and despite that fact, these people really supported that effort.

I have a little feeling in that regard that fair is fair in regard to what we did in behalf of corn country. The drought continues in this country; 50 percent more rainfall last year, 10 or 20 percent this year. So what we did for corn country was right, under the circumstances, and we saved a lot of farmers and ranchers, and it is only fair that we have that as of this year for wheat country.

I realize that we have some problems with the budget. Jim is on the Budget Committee, and that is a tough job, and I realize we have some problems with some crop insurance policy. We have a commission studying that. We have two fine Kansans on the commission. We have 26 recommendations already and we will get to that. It has not worked very well out in this country. But it is going to take 2 years to get that on board, and with all due respect to the crop insurance debate and all due respect to the budget, the savings and the deficiency payment should be applied to disaster assessments.

And one more thing, as the fat person said as they crawled through the barbed wire fence, "One more point and I am through." It is my district, give me a little while. These disaster bills come in even-numbered years. The disaster assistance came when there was a Governor's race in Texas; and disaster assistance came last year during the campaign for President. You had Mike Dukakis wandering down one corn row and George Bush coming up the other one, and Willie Nelson singing a concert at the State fairgrounds. We have the horsepower in this room and we have the horsepower with you as chairman and me as one of the ranking minority members on the subcommittee, and Senator Dole and Senator Kassebaum and the good support of the Governor and the entire Kansas Congressional Delegation. Let us get the job done.

I want to pay the Governor a compliment. When he got on the phone to me several weeks ago, I guess it has been more than that, and you said, "How on Earth can we get this hay and grazing and get the emergency feed assistance and the additional assistance that you asked for last week with the Secretary of Agriculture for the livestock producer." I said, "I don't know how you are going to do it, Mike, because we do not have anybody on board in the USDA. People are—faster than Bush is getting these people on board back in the USDA." And you said, "Let's get the Secretary out." So we moved on that, the Secretary did come out, we did get the assistance, and I will tell you that it is my prediction that as of next week, the Secretary will be making an announcement along the lines that have been recommended by the National Cattlemen and Livestock Producers about the possibility of hay and grazing on CRP grounds, and also for transportation assistance, also for some loan money, and I think that is about the extent of it, but I know the Secretary will be in touch with you and thank you for jumping on this thing early so we at least got the Secretary out here to take a firsthand look.

One last thing, I would like to introduce you to, Mr. Leon Torline. The reason I am introducing Leon, and I should introduce Mr. Bart Boyd of the Ford County Wheat Growers. I would also like permission to insert a statement from the Four County Wheat Growers at this time, Mr. Chairman.

[The prepared statement of the Ford County Wheat Growers appears at the conclusion of the hearing.]

Mr. ROBERTS. The reason I am introducing Leon, we have heard a lot of people talk about substitution and base flexibility. We are into all sorts of discussions on that, and every one of us has that now as No. 1 in terms of our farm program suggestion in regard to the new farm bill. This is the gentleman, and it was the Ford County Wheat Growers that sat me down 5 or 6 years ago trying to get some base flexibility, trying to get us to the point where you do not put the seed in the ground according to your acreage base but according to the market. Mr. Torline worked with Raleigh Stukenholtz of Servi-Tech out there in Dodge and others. He has an outstanding statement along with the Ford County Wheat Growers on what we ought to be doing in this regard and I want to give him credit.

Dan, you have heard me make the substitution speech. This gentleman was the godfather of that effort along with the Ford County Wheat Growers.

Thank you all for coming. It is a pleasure to be here.

OPENING STATEMENT OF HON. JIM SLATTERY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF KANSAS

Mr. SLATTERY. Mr. Chairman, Pat, it is really a pleasure to be here today. I do not make it out here in the first district, in what Pat Roberts and the Hutch News calls real Kansas, as often as I would like to, but if I thought I could bring more rain I would come more frequently. It is good to see you all here this morning.

I have observed that we oftentimes have these kind of hearings only to see very little action result at those hearings. We are endlessly involved in collecting information it seems like in Washington these days, but I think this hearing is going to be different. I think that Dan and Pat have been very accurate in pointing out that we are going to have some action resulting from this hearing. We are going to have, in my opinion, some real decent disaster assistance. I think the budget that the Congress recently approved will make room in sort of a grudging way for disaster assistance. It looks like maybe the savings that will result from increased prices hopefully will be enough to offset the cost of the disaster assistance when the cost of deficiency payments go down, so I am confident, from a budgetary standpoint, that we are going to be able to make room for the kind of disaster assistance that we need.

I am going to be very brief, Dan and Pat, because I want to get into hearing from the Governor and I know his schedule is real busy and you folks probably want to get on with your Saturday afternoon.

But one of the things that I am really concerned about is what we can do to make this crop insurance program work better. Obviously it is not working in many parts of the country. It seems to me that we really need to develop an actuarily sound crop insurance program, if this is possible, so that in the future farmers will be able to conduct their business as businesses, and make a decision early on in the year as to whether they want to buy a sensible crop insurance policy or not. The Government needs, in my opinion, in the future, to be in a position where there is a crop insurance program in place that will eliminate the need for this sort of a political response to these problems that arise in different parts of the country.

I would really like to hear from those people testifying today as to how they think we can make the crop insurance program work better right here in Kansas. I think over the long term it is going to be important for us to have that kind of program in place. I am concerned that these annual responses to crises that develop in different parts of the country are going to become increasingly difficult to sustain from a political standpoint.

On the question of substitution, in my part of the country up in northeast Kansas, this has really been a headache for us and I am sure it is out here for you all, also. It just does not make any sense to me at all, that we have in place a policy that basically makes it more difficult for farmers to manage their farms and to rotate crops in a sensible fashion. It seems to me that when we talk about the 1990 farm bill, certainly substitution and more sensible management tools for farmers are absolutely essential.

The other point that I am concerned about is in addition to responding to the obvious disaster we have with our winter wheat crop, I think it is also important for us to be taking a look at where we are going to be with our feed grain crops. In my part of the country frankly, up in northeast Kansas, we did not get a lot of the rain that you did here in the last few weeks. So we are in some of the driest parts of the country, right up in northeast Kansas.

It is good to be here today and I am looking forward to hearing all the testimony. I hope we can focus on some of the issues that I have just talked about and all the other issues, too, that have been mentioned by Pat and Dan.

Gentlemen, I wish that I was a member of the Ag Committee. But I have to bite the apple on the Budget Committee occasionally.

Mr. GLICKMAN. I might say parenthetically, this is the first hearing I have ever been at where there is a giant canyon between the audience and the folks up here. We may fill it with water, Governor.

It is a pleasure to welcome the Governor of Kansas, Mike Hayden, along with Lois Schlickau, a constituent of mine who is the chairperson of the State board of agriculture, and Sam Brownback who is the secretary of agriculture. We are delighted to have you here and we thank you for your help so far in this area, and you may proceed.

STATEMENT OF MIKE HAYDEN, GOVERNOR, STATE OF KANSAS

Governor HAYDEN. Thank you, Mr. Chairman. We appreciate very much, you, Congressman Roberts, and Congressman Slattery being here in west central Kansas today and taking the time as you did in Texas yesterday to hear from our agricultural producers in the heartland of this country.

We also appreciate you bringing the showers this morning. I do not want you to get overoptimistic about those, because I heard recently that the Kansas wheat crop is much like Pat Roberts' hair cut. The disaster has already occurred.

Mr. ROBERTS. Mr. Governor, in my case I am operating with a 50 percent set aside.

Governor HAYDEN. You—for CRP, I will tell you that. [Laughter.]

We do appreciate you being here today and we are encouraged very much by the action of some of the Senators, especially Senator Dole and Senator Kassebaum yesterday, and we are very appreciative of the fact that you realize the massive impact on the farm economy and on our rural communities that this drought has had.

There has been, we feel, in Washington an underestimation. Not on the part, certainly of our legislators here today, but on the part of the USDA and the national media. An underestimation of the farm losses that are going to occur in wheat country in 1989.

We predict conservatively, conservatively, that farm losses due to the poor wheat crop in Kansas are likely, in fact very likely, to exceed $800 million in Kansas in 1989. That is based on the report that was based on May 1 crop reports. Those have been revised downward as you know yesterday, to where the current crop is estimated to barely exceed 190 million bushels. That is compared to many years in which we have harvested 400 million.

So it is, as Congressman Roberts has said, a 50- to 60-percent loss, and it is devastating, especially to our rural areas, our agribusiness community, and our producers.

We have also seen a very negative impact, and we have not heard enough about this really in Washington, a very negative impact on the beef-cattle industry. Kansas is the No. 1 processor of red meat. We are the No. 2 producer of red meat in the country. Beef provides more than half of the cash receipts to Kansas agriculture. We have seen a liquidation of cow herds in unprecedented numbers in recent times. Our ponds are dry, our hay is virtually gone, what was left over from last year, and our fields are vulnerable to wind erosion.

We do not, as Kansans, as an independent people, we do not relish asking the Federal Government for help. We do not relish that at all. But the reality is that in terms of agricultural programs and assistance to our farmers, most of the action is at the Federal level. We know that, you know that, and we are glad that you are here today to extend a helping hand to our producers.

We are experiencing our own demand at the State level related to the drought. In fact last July, nearly 1 year ago, we formed the Governor's drought response team that has met regularly to coordinate State, local, and Federal activities. In addition to agriculture, we are facing at the State level, concerns in public and domestic water supply, minimum stream flow, deteriorating water quality, high fire hazards, and a myriad of other drought-related problems. State and local resources are strained to meet these problems. In fact several smalltowns in Kansas have already run completely out of water.

As you know, I, Sam, and Lois, and many others have been very aggressive in requesting drought assistance for Kansas, and we appreciate the Members of Congress who work so closely with us and Secretary Yeutter in requesting assistance available through his discretionary powers, and in many cases he has been quite responsive.

For example, he provided quick response to those counties meeting loss eligibility criteria in the Emergency Feed Assistance Program, and there are nearly 90 of those that have been approved. And in the emergency hay and grazing of acreage conservation reserve and in conserving use acres. So we appreciate what you have done for us so far in working with the Secretary.

Also the Governors of the drought-plagued States will continue to work with Secretary Yeutter, in fact we have been on the phone with him this week, to achieve the full range of assistance available under his authority. Our major need for drought relief lies outside the discretionary authority of the Secretary. It will in fact require congressional action. Our major need is for extension of the Drought Assistance Act of 1988, to apply to winter wheat planted in 1988 for harvest in 1989. That is the chief provision of drought-relief legislation that we would urge you to adopt in this session of Congress. The need is obvious.

I would like to add here that, the most welcome rainfall we have received is far too late to really impact most of our wheat producers, except in the extreme western parts of the state. The extreme conditions of last fall, winter, and this spring, have already done irreparable damage and the situation continues to deteriorate.

As Congressman Slattery alluded to, the President's 1990 budget projected $1 billion for payment to wheat producers for deficiency. It is now projected that there will be substantial reduction or possibly even elimination in deficiency payments because of the higher prices. Projections from USDA indicate that application of the 1988 Disaster Assistance Act to the 1989 crop as we are requesting, would result in disaster payments of between $250 to $350 million. We think it is affordable, within the budget targets that Congress has set, and will even allow some money to be left over for budget reconciliation.

To apply a portion of the deficiency payment savings to wheat farmers only seems fair to us, especially in a drought situation like we have on our hands today.

There are three other items that we are requesting that would be of real assistance to Kansas farmers and ranchers. One has been alluded to by Congressman Roberts and that is that haying of CRP acreage be allowed within guidelines that minimize negative environmental impact on our natural resources. This acreage would provide much needed forage for our hard-pressed livestock producers. But one thing I urge you to do in adopting this legislation, in talking with other Governors, is to develop the guidelines on a State by State basis. Conditions in South Dakota are not the same as they are in Kansas. Please give us the flexibility of State by State guidelines.

The next thing we ask is to provide cost sharing on water enhancement projects to allow livestock producers to improve their long-term water supply capabilities.

Last, implementation of Federal cost-sharing assistance to transport livestock to emergency pastures in areas where rain has occurred.

We very much appreciate your coming to Kansas and to hear first hand about these problems. Kansas farmers and ranchers are resilient and proud people, and they are independent, and they have weathered hard times before and they probably will again. However, today we are asking the consideration of the USDA and the U.S. Congress to assist them through the worst drought conditions in this State in over 27 years.

Thank you for your kindness, for your courtesy, and we are looking forward to your positive response.

[The prepared statement of Governor Hayden appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you. Next, Ms. Schlickau.

STATEMENT OF LOIS R. SCHLICKAU, PRESIDENT, KANSAS STATE BOARD OF AGRICULTURE

Ms. SCHLICKAU. Good morning, and thank you, Mr. Chairman, for allowing me to testify this morning. My name is Lois Schlickau. I am president of the Kansas State Board of Agriculture, and I am also a farmer from Haven, KS.

I might mention that I am very pleased to have Chairman Glickman as my Congressman, and we are most appreciative of his efforts and the efforts of our other Congressmen for their work on behalf of agriculture.

My presentation is going to be short and specific. I am not going to cover the factual setting of the situation, but instead will leave that to others who will be testifying.

Kansas is in the midst of one of the worst droughts we have faced in this century. The Kansas State Board of Agriculture believes it to be imperative that a Drought Relief Act be enacted by Congress to lessen the catastrophic impact this drought is having on our farmers, our ranchers, and the economy of this State.

On April 4, 1989 the Kansas State Board of Agriculture voted to seek and support legislation for drought relief from the U.S. Congress. We are requesting extension of the 1988 Disaster Assistance Act to apply to all crops harvested in 1989.

As Kansans we are used to dealing with the vagaries of Kansas weather, and we often deal with conditions that are less than hospitable. However, the situation we are currently experiencing is abnormally severe. This week we have been blessed with some welcome rain, but this is only a temporary reprieve unless significant amounts of moisture are received. Although we have some surface moisture, the subsoil moisture is still dry and not adequate to continue growing spring planted crops.

This does not appear in my printed testimony but I would like to briefly share with you the situation on our farm. We have pastures in the south central area of the State as well as in the central area. In the south central area, our grass is short and sparse. In the Flint Hill area our grass is in much better condition, but we have no water. Our ponds are completely dry.

We raise about 250 acres of alfalfa to feed to our cattle for winter feed. Our alfalfa is just not growing this spring. In fact we have turned cattle out on portions of our alfalfa fields in order to try to utilize some good from the crop.

Our wheat crop is short, weak, and the stands are thin. The wheat in our area is headed and the wheat heads appear to be about average in length, but the heads are not filled out well. In our area we will have some wheat to harvest and I know there are some areas of the State where there will be none to harvest, but we do expect our yield to be significantly lower this year.

That is just a quick overview of the situation on our farm, but it is typical of the entire south central area of the State.

Most of Kansas needs drought relief assistance along the lines that we passed in 1988. The drought of 1989 is just as severe if not more severe than the drought of 1988.

We urge congressional support in passage of an extension of the 1988 Drought Assistance Act to all crops harvested in 1989.

Thank you for your consideration.

[The prepared statement of Ms. Schlickau appears at the conclusion of the hearing.]

STATEMENT OF SAM D. BROWNBACK, SECRETARY OF AGRICULTURE, KANSAS STATE BOARD OF AGRICULTURE

Mr. BROWNBACK. Mr. Chairman, it is a pleasure to be here. My name is Sam Brownback, secretary of agriculture, State of Kansas.

I will confine my statements, Mr. Chairman, to the factual conditions facing Kansas agriculture due to this extended drought.

The conditions are as follows: The Kansas wheat crop was rated by the Kansas Agricultural Statistics Service as of May 1, 1989 at 202.4 million bushels. This yield would be from a projected harvested acreage of 9.2 million acres, that of 12.4 million acres that were planted last fall. Average yield per acre is expected to be 22 bushels, down 12 bushels from 1988 and the lowest yield since 1967. This year's wheat would be the smallest crop since 1966. The average tiller count from the wheat objective yield survey was the lowest since 1977 and the second lowest on record.

I would further note that this projection was as of May 1, and was based on the assumption of normal weather patterns from May 1. Despite some welcome rains recently, most parts of the State have not received normal weather patterns since that May 1 date, nor do many people now expect weather to return to normal; thus, I believe these projections to be on the high side.

The wheat condition as of May 15, 1989, as determined by the Kansas Ag Statistics and the county agents of the State found that 62 percent of the wheat is rated very poor, 23 percent was rated poor, only 2 percent of the wheat is rated good and 2 percent in excellent condition. This is the lowest condition rating of the wheat since those records have been kept. The lowest condition since they've been kept.

Much of the wheat in the State is very short. Stands in the central and north central parts of the State are heading out at only 10 to 15 inches high, some shorter than that, and will be nearly impossible to harvest in some cases. Furthermore, Wheat Streak Mosaic symptoms are becoming more apparent and will clearly exacerbate the situation. Wheat heading is at 70 percent. That is 25 percent above last year and 25 percent above the 5-year average. It appears certain we are going to have an early, very small crop.

The 1989 wheat crop was planted under generally short surface and subsurface moisture conditions last fall. Many stands managed to sprout and emerge before going into dormancy with little or no secondary root development. A generally mild winter with below normal rainfall caused some of the stands to break dormancy early. Subzero temperatures blanketed the State in early February and killed much of the top growth. As the wheat crop later broke dormancy in March, widespread winter kill became more evident. Continual subnormal rainfall with some record high temperatures has stressed the crop even further. The only calamity that this wheat crop has not experienced to date has been extensive hail across the State. I made that point in Beloit, KS to some farmers there and a fellow held his hand up quickly and said, "We would sure like to see that hail. We could sure use the moisture."

April rainfall in Kansas was 19 percent of normal; the accumulated July 1988 to April 1989 precipitation, which of course is what the wheat crop is going to grow off of for that timeframe, the precipitation was the lowest since 1956 and one of the lowest in the last 50 years.

Surface moisture as of May 15, was rated 1 percent adequate and 99 percent short. Subsurface moisture at that same date was rated zero percent adequate and 100 percent short. There is no subsurface moisture in this State.

Statewide the May 1 pasture conditions averaged 47 percent of normal, the second lowest on record. The lowest since 1935. Conditions ranged from only 27 percent of normal in north central Kansas to 70 percent of normal in southeast Kansas. One year ago today pasture conditions were rated 84 percent of normal. Again, they are rated 47 percent of normal today.

Hay supplies and grass availability are extremely short. Callers representing more than 30,000 cow/calf pairs have called the grass and forage hotline in the 3 weeks that that hotline has been in existence. The hotline has been converted to a national 800 number now, in hopes of locating more pasture and hay supplies nationwide. I might point out there as well, Mr. Chairman, when I checked Thursday on that grass and forage hotline, we had received something like 8 calls from instate of pasture available instate. So we are exceedingly short and a lot of people are moving cows.

Hay production was down 14 percent in 1988 compared with 1987 and with little wheat pasture and limited growth of grass, the May 1, 1989 hay stocks were down to 14 percent of 1988 production, with a total about 29 percent below year-ago levels. Hay has been selling at record high prices.

Recent placements of cattle on feed have been at record levels in Kansas, with first quarter placements in the 13 major feeding States the highest in 18 years. May 1 cattle on feed in Kansas stood at a record high of 1.71 million head, up 16 percent from the previous year. Some, as well, due to the drought conditions and lack of grass and forage.

Kansas has seen a seven-fold increase in the numbers of cows going to slaughter in federally inspected plants. On April 8, 1,400 head were sent to slaughter in Kansas. Many are slaughtered out of the State. During the same timeframe in 1988, 200 to 300 head of cows would have gone to slaughter, so we had a seven-fold increase. Regional sale barn testing for brucellosis shows 7,000 head tested on Monday, May 8, 1989 as compared with normally about a 2,500 head daily average. So, up two to three times increase of that cow testing for brucellosis.

The Federal/State brucellosis laboratory on May 9, 1989 showed 8,561 brucellosis tests compared with testing a year ago at half of that, a little over 4,000. The brucellosis testing reflects sales of cows and/or movement of cows to other States for pasture, so we are seeing a massive movement of cowherds.

As of May 1989 there were more than 8 million acres in Kansas in a condition to blow, as rated by the Soil Conservation Service. That compares to less than 500,000 in a similar condition in May 1985. Almost 5 million acres in Kansas were damaged due to wind erosion through May 1989 compared to less than 300,000 during the same period in 1985. Massive wind damage.

As of May 12, 33 communities and/or rural water districts in the State were experiencing, or had experienced some rationing of water in 1989. That number is expected to rise substantially if the drought continues, many of those in Mr. Slattery's district in northeast Kansas.

Many streams are flowing at 1 to 16 percent of normal for May, and this rating as of May 12, 1989 from the Kansas Water Office.

Eighty-nine counties were approved by the ASCS for either or all of the following programs: emergency feed program, emergency feed assistance program, and emergency haying and grazing program.

On April 17, 1989 a letter was sent from the Governor to Secretary Yeutter requesting emergency feed assistance for the State livestock producers.

On April 20, 1989 Governor Hayden requested that Secretary Yeutter declare that a natural disaster existed across Kansas except for 15 counties in southeast Kansas. This request would allow us to get the low-interest loans from Farmers Home Administration. That is still being studied by the USDA.

Mr. Chairman, those are the facts as we know them today. It is a grim, critical condition facing Kansas agriculture. Assistance is needed and warranted from the Federal Government for our producers. We implore you to help us through this devastating natural disaster.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Brownback appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you all for your excellent statements. I appreciate the specific numbers you gave us, particularly on the water issues which is something we often lose sight of.

I am reminded of the story about hail to get precipitation, I was down in Texas and somebody was talking about freeze damage, that the hail was so great outside of Amarillo, there was 4 inches of it on top of a bunch of grain they had outside and they said the freeze was just awful on that.

I just want to ask one question to make sure that there is complete unanimity among you all. In the Governor's statement, you talk about obviously the highest need is to extend the drought assistance plan to winter wheat. Lois' statement talks about for all crops harvested.

In checking with staff I found out that even though the bulk of last year's disaster applies to disaster corn in corn country, 20 percent of Kansas wheat producers did take advantage of that last year's disaster bill, so it did have some applicability in this State. I just want to make sure whether you are in agreement on this or there is something that perhaps I am missing here.

Governor HAYDEN. Mr. Chairman, there is no disagreement. Lois is reflecting the official action of the State Board of Agriculture when they voted that it be applied to all crops. We look at the situation as related to the other Governors. We also had the conversation with Secretary Yeutter and of course with members of our congressional delegation and looked at our greatest need, which is wheat. No doubt about it, the damage has already occurred. Milo and corn, a lot of our corn in Kansas is irrigated, especially in the western part of the State. Most of the corn disaster occurred up in Congressman Slattery's district last year and they are still poised to have another disaster up there if it doesn't rain soon.

But in talking to the Secretary and Members of Congress, they said we can document the wheat. It has already happened. We are far more likely to get some help there. I notice in the bill that both Senators Dole and Kassebaum endorsed yesterday it applies to the wheat crop because they felt like they could document that and get it substantiated through the Congress.

So we are in favor of all crops. Our greatest need is the wheat crop because the disaster has already happened.

Mr. GLICKMAN. But it is the position of the State Board that it be applied to all crops?

Governor HAYDEN. That is the formal position of the State Board of Agriculture.

Mr. GLICKMAN. If it were applied to wheat only, it would depend on how you were to define it. If we were just talking about this 1988 crop only, we would want to make sure that—applicable to alfalfa or perennial crops that are not necessarily planted every single year. That would be a tremendous loophole if they were not covered under that arrangement.

Governor HAYDEN. They should be covered. Our statement says, "or any crop planted in 1988 for harvest in 1989." Obviously some of that alfalfa was planted in 1987, some in 1986 and some in 1985, but it was for harvest in 1989, so we want to make sure, if we were not clear, that those kinds of crops should be covered.

Mr. GLICKMAN. Thank you all for testifying. I am finished.

Mr. ROBERTS. I would just like to make a comment in reference to the legislation that is now before the Congress, Governor. I do really appreciate your clarification of where the State Board is and where the State is.

Over 1 month ago Gene—introduced a very crop specific bill, that is winter wheat. Since that time there have been several bills introduced on the House side, and now, as I indicated in my earlier comments, a very dramatic show of force on the part of many Senators from many States. What your position is, and it seems to me that we can do a pretty fast job here in this next week, maybe even Tuesday, with the leadership of the House Ag Committee to determine what bill it will be.

I would hope that whatever bill we are able to agree upon will be very close to your position and very close to the bill that has been introduced by Senator Dole, Senator Kassebaum, Senator Bensen, and Senator Boren.

The Senate is out of session as of this next week, but it seems to me that we are looking at about a 2-week timeframe because obviously you have a sign-up deadline with regards to—and by the way, that contract would have to be waived, Mr. Chairman, in any disaster bill if that were the case. But expeditious movement of these bills is exceedingly important, and I would not think it would be that difficult, given the number of bills we have, to reconcile those differences quickly and reflect what the Governor has suggested, and move.

Mr. GLICKMAN. Thank you. Mr. Slattery.

Mr. SLATTERY. Two things. I have a question and a comment. The comment is that I happen to believe that whatever we do needs to be broad enough to cover feed grain quality of the crops too. In my part of the country, if we do not get rain soon, northeast Kansas may be the driest part of the State. So I think whatever we do needs to cover feed grains and the other crops.

I think Dan and Pat, you are absolutely correct when you assert that we should be moving quickly. I will tell you another reason. Right now, there is a view in Washington that we have met the $100 billion Gramm-Rudman deficit reduction target. That is a falsehood. We have not done that. The budget resolution that has been passed is based on some very, very rosy economic assumptions that are not going to come to pass. This fall, I predict, that we are going to have a real budgetary donnybrook. I think it is important for us to move as quickly as we can, and done within the context of the money we have available. I am confident there will be adequate money available within the USDA budget to respond to it, but it is important that we get this done before the August recess and before we get into what I predict, will be a real budget showdown this fall. If we get into that, and if we think we can come back this fall and deal with the feed grains issue, I think it is politically going to be much more difficult for us to do that if we are into an overall budget debate this fall when it becomes very obvious to everyone that we have not reached the Gramm-Rudman deficit reduction target. So that is another reason why we need to move quickly.

The question I have goes to the CRP acres and I am just curious, we are all very concerned about this livestock situation. It is one thing to lose a crop and another thing to have to sell the livestock herd that you have spent years developing. I am very alarmed that obviously that is going on. I am just concerned because, Is there a significant amount of this CRP acreage that can in fact be used for decent haying and grazing? Does anyone have a handle on that? I am just curious. We are all talking about urging the Secretary to use his discretion to give us more authority to use that CRP land, But is there anything out there, I guess, is my question. Do we have a handle on that?

Governor **Hayden**. We have nearly 2 million acres statewide. Now of course some of those acres were seeded 3 years ago, some of them 2 years ago, some of them last year. The stands vary considerably, as you can imagine, and during a drought many of those stands did not get very well established.

There are some cases, especially in your district and on south of your district in the fifth district, where in fact cool season grasses, the bromes and the fescues did get a fairly decent stand and with some recent rains this spring have produced some good forage at this point.

Mr. **Slattery**. I am familiar with the situation in this part of the country. I know what it is up there. But I am just curious how the central Kansas, western Kansas, is there any——

Governor **Hayden**. Out here of course most of the acres are seeded in native grass. There is some brome and some fescue, but not much. Most of it is native grass. Of course it is the most highly erodible land. It has to be to qualify for CRP, or sandy as it is in southwest. Most of those stands are not very well established because of the drought.

If a stand is well established, we are recommending that it in fact be grazed after June 20, when the forage value of the warm season grasses really starts to come into play. Right now there has not been much growth on them and the forage value of course is not very much. With some of the recent rains we hope it will be something before too long. But the truth is the forage value on most of those acres is pretty limited, Jim, because the drought has really set them back.

Mr. **Brownback**. My only comment to that would be that right now we are so forage and grass short in the State that anything we can find to help out that livestock producer from shipping that cattle out, from selling them, which they are doing right now, because of the stress in that situation, anything we can find we should do to help the livestock producer of this State.

Mr. ROBERTS. I would tell my colleagues and the Governor that it is my expectation that the Secretary will announce haying as of next week on the CRP acres.

I would also say that there is a debate, let us be very frank, within the administration, as to whether to allow grazing. Quite frankly the USDA is on our side and also quite frankly there are some at the White House level and the OMB level who feel like that might be a problem in regard to the environmental concern. I think we can push it over and I think we can get it done next week.

Mr. GLICKMAN. We thank you all very much. It was very useful testimony. We appreciate you being here. We hope to get something done on this soon.

The next panel is composed of Mike Smith, president of Weather-Data Inc., in Wichita, formerly a TV star, channel 3. Maybe still is. Dr. Jim Shroyer, agronomist, Kansas State University, Manhattan, KS, and Mr. Rollie Stukenholtz, president, Servi-Tech, Inc., Dodge City, KS.

We are delighted to have you here. I would say that this panel is here to try to give us an idea about weather, the environmental and the climate picture for both short term and long term.

I would just make a comment before we begin, and I am delighted that all three have agreed to appear. Mike Smith is an extraordinary human being, and he happens to know that I have similar feelings about the weather as he does. That is, I get a kick out of the weather. It is of great interest to me.

In fact Jim Slattery and I were talking, and I have been known to watch on cable television the weather channel for hours at a time and my wife thinks there is something wrong with me. But not only does he care about the weather, he is interested in it in terms of its effect on us. He has become one of the nationally leading meteorologists in the country and in the world. If he were heading up the USDA's weather system instead of what is there, I would guarantee you the information flow would be a lot more accurate.

Mike provides weather information to newspapers and to people, businesses all over the United States and around the world, so we are delighted that he is here and that he can offer some of his thoughts about climate conditions. So Mike, we will begin with you. We are glad you are here.

STATEMENT OF MICHAEL R. SMITH, PRESIDENT, WEATHERDATA, INC.

Mr. SMITH. Thank you, Mr. Chairman.

I appreciate the invitation from the subcommittee to appear today and I would like to present some information on the status of the drought and some thoughts on the strategies to help minimize the effects of drought on agriculture in the future.

I have a number of Vu-Graphs to present along with my testimony today. These are all reproduced in the written testimony.

The first Vu-Graph shows the status of the drought 10 months ago midway through the summer of 1988. The shaded areas are regions where the Palmer Hydrologic Drought Index indicated "severe" or "extreme" drought. The PHDI is used by meteorologists, hydrologists, and climatologists to measure the intensity and severity of drought. At that time, the worst conditions were found in the northern plains and in parts of southeast Iowa and western Illinois. The two latter areas reported less precipitation from April through June than at any time since records began being kept around 1895. Nationwide, the percentage of the Nation experiencing extreme drought was 43 percent, the fourth highest value in history. It compares with 44 percent in 1936 and 45 percent in July 1954. Only July 1934 with 61 percent of the Nation experiencing severe or extreme drought, had significantly worse conditions.

Since October, plentiful rains have fallen in most of the eastern Corn Belt, the Cotton Belt, and the delta soybean region, greatly easing the drought in those areas. However, Kansas and the area immediately surrounding Kansas had a dry summer and fall. The winter was one of the driest in history, followed by a dry spring.

The second Vu-Graph shows that the drought has migrated southwest since last summer. Extreme drought conditions are now present from Kansas into southeast Iowa as shown by the Palmer index figures from last Saturday, which are the latest figures available. Extreme drought is also occurring over the Southwest United States. The Palmer index defines values of minus 4 as extreme drought. Middle and nor[illegible]st Kansas and southern Iowa have values lower than minus 5.4, which are disaster conditions.

Beneficial rains have fallen in the central plains since last Saturday when these readings were taken. The next graphic shows the rainfall this past week. Amounts in the 4- to 6-inch range have fallen over southwest Kansas, the eastern Oklahoma Panhandle and the northeast Texas Panhandle. Substantial rains have fallen in most of Kansas and Oklahoma, but note that amounts were relatively light in Iowa, eastern Missouri, and northern and eastern Nebraska.

While these rains have been beneficial, much more rain is needed to eliminate the drought. In southern Iowa, it would take 10 to 15 inches to eliminate the drought in a single month. In Kansas, the amount needed to eliminate the drought range from 6 to 10 inches, even factoring in these most recent rains.

When might further relief be expected? I think it is likely that the central plains will have near normal rainfall the next 15 to 30 days. Of course that will not help the wheat crop, but that will most likely keep the drought from getting worse. There should be adequate moisture for newly planted summer crops in the southwest half of Kansas, parts of Texas and Oklahoma, but other areas are still very much in doubt.

In order to look farther into the future, it is necessary to attempt to understand what has caused the drought. There is no doubt that this drought has been caused by an abnormally large and persistent high pressure system that has lingered over the Central and Southwest United States for more than a year. The high deflects the jet stream and the storms that move along the jet stream away from the Central States. Fewer storms translate into fewer opportunities for rain than would normally occur. Plus, a high of this nature causes warmer than normal temperatures which drive up evaporation rates.

Why has the high been so persistent? On this point, opinions diverge. My personal opinion is that the high has partially been held in place due to an unusually cold body of water in the Pacific between South America and Christmas Island. This colder than average water has come to be known as La Nina. The combination of the cold water to the south and warm water in the central Pacific have caused the jet stream to be diverted farther north than normal over the middle Pacific. Atmospheric theory shows that abnormalities in the jet stream in one area of the hemisphere can cause abnormalities in other areas of the hemisphere. The high pressure and the unusual jet stream configuration over North America are related to the abnormalities in the Pacific.

Also contributing to the drought's persistence is the dry soil. Once the soil becomes very dry, less evaporative moisture is added to the lower atmosphere. The Sun bakes the dry soil, helping to cause afternoon temperatures to be warmer than normal. Less moisture and lower evaporation lead to lower relative humidities which make it more difficult for the atmosphere to produce rain.

Weather forecasting beyond 30 days is highly imperfect. The official National Weather Service outlook for June and July calls for near normal rainfall in the western halves of Kansas and Nebraska and all of Oklahoma and Texas. Drier than average weather is forecast for Iowa, Missouri, and the eastern halves of Nebraska and Kansas. That forecast may turn out to be correct.

A study by Thomas Karl of the National Climatic Data Center shows that droughts are unlikely to be broken in June or July in the Central United States. Statistically, as this Vu-Graph shows, it is much more likely for a drought to be broken between August and October.

In reviewing all the data available to me, I think we will see near normal rainfall in late June and July. If that is correct, the drought situation will change little from a hydrologic standpoint. Ponds and rivers will continue at below normal levels. Summer crops will probably do relatively well in the areas that received the recent heavy rains, but parts of northern Missouri, Iowa, northeast and north central Kansas and northwest Texas will continue to have significant to serious problems.

As the La Nina has weakened and shows signs of disappearing altogether, I think there is a good chance the situation will have greatly improved by October or November, which would be good news for the 1990 winter wheat crop.

What might we do to minimize the effects of future droughts on farmers?

We do not know why the cold water formed or why it has been so persistent. This research needs to be done. Research is also needed on the correlations between solar cycles and droughts and possible correlations between the amount of stratospheric volcanic dust and drought. If these correlations do exist, we should then try to find ways to use this information to predict when droughts are most likely to occur.

The United States needs to catch up with most of the rest of the world and install state of the art supercomputers at its National Meteorological Center to allow meteorologists to make better forecasts in the 4- to 10-day range. This would benefit the entire economy, not just agriculture.

More and better agricultural weather information is also needed. Information on evaporation, soil temperatures, and solar radiation is needed in a unified, timely basis so meteorologists can make better agri-weather forecasts.

Some of the remarks made here today indicate some of the problems in having to rely on Government meteorologists to come up with agricultural weather information. If Congress will resolve the uncertainty that has been hanging over the role of Government versus the private sector in agricultural meteorology, private companies would be in a position to provide high quality, timely, and cost effective weather and climate forecasting services to all phases of agribusiness, including individual farmers. Farmers could then become more efficient and productive with this information.

Thank you for the opportunity to express my views. I would be pleased to answer any questions you might have.

[The prepared statement of Mr. Smith appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much. Before we have questions we will move on to Dr. Shroyer, Kansas State University. We appreciate you being here.

STATEMENT OF JAMES P. SHROYER, EXTENSION SPECIALIST, CROP PRODUCTION, KANSAS STATE UNIVERSITY

Mr. SHROYER. I am Jim Shroyer, extension agronomist at Kansas State University. I want to thank the chairman of the subcommittee for allowing me to speak today on the effect of the drought in Kansas.

[Slide presentation.]

Just to reiterate what Mike said, to show you the drought conditions across the State, late snow in the northwest and adequate rainfall in the southeast, those are the best situations as far as the wheat goes. The hatching that you see in the center there is what we call poor to very poor. This is my rendition of the condition of the wheat crop.

In the eastern third of the State we grow about 1.2, maybe 1.4 million acres this year. I was talking to the area agronomist in the southeast, and he said that if it did not rain this week, and that was on Monday or Tuesday, if it did not rain this week we would produce half a crop in that area that we consider as good. So, those producers in the southeast are never 2 weeks away from a drought or a flood.

It is amazing to see that the crop has done so well when we normally think that a wheat crop takes 10 inches of moisture just to get it to heading. This year we have seen the wheat crop go from planting, emergence, and heading, in a relatively short period of time with half that amount of rainfall. The effect on yields are obviously quite great.

These are the percent of normal precipitation on a 6 month percent of normal for the past 12 months. You can see that we are well behind normal, and this has a major effect on crops.

The drought has a long tail. What I am going to talk to you about today is the effect on crops, rangeland, local businesses, and soil erosion as well. Governor Hayden mentioned all those facts, so I should go through these pretty quickly.

On crops, this sordid affair started last summer and last fall, when planting conditions were very very poor, with lack of subsoil moisture and surface moisture, so that we got erratic emergence. The seeds had germinated but had not emerged. Several farmers in this particular case planted the second time only to have the crop come up in the spring time. In those situations we can, as agronomists, say that a maximum yield would probably be 22 to 24 bushel per acre no matter what happens with the best of weather conditions.

This is one of the first times I have ever seen irrigated wheat be chiseled, but due to the lush growth in December and January followed by nearly a 100-degree drop on February 1 and then warming up again in late February and then again another tremendous drop in early March, this caused severe damage to the irrigated wheat.

Finally, this whole affair on the wheat crop has gone on, high temperatures, very low temperatures, lack of rainfall, and finally the last of April, first of May we had 22-, 26-, 28-degree temperatures across the State when the crop was in a very vulnerable stage of growth. This field in particular was on the Hodgeman/Pawnee County border, and suffered severe freeze damage similar to 1981. I think we will see more freeze damage showing up north of that area in the next week or so.

This picture was taken just 2 or 3 days ago in north central Kansas. The wheat had finally just given up the ghost, so to speak.

Of the 12.4 million acres of wheat that we have planted this year, I think it is safe to say that over 11 million acres have been affected some way by the drought or the freezing conditions and winter kill. I think that is a safe statement. Even in those areas of the State that I have shown on the hatching there, those stands are 75 to 85 percent of normal and they will be very pleased to get 35 or 40 bushels per acre when they normally would be expecting 50 to 60 bushels an acre.

So I am predicting with, looking at the planted acres and our long-term trends in this past decade, excluding 1981 and last year due to wheat streak mosaic, our trends were approaching 40 bushels per acre, so it was within the possibility, if we had had subsoil moisture, surface moisture, we could have been pushing 450 to 480 million bushels, so that a loss of $600 to $800 million to the State is within the realm of possibility.

The drought does not stop there, as has been mentioned before. This is alfalfa, or was alfalfa. I think we have lost pretty much of our first crop, our first cutting on dry land across the State, and our irrigated acres, and I think Rollie will testify to that too, is that those irrigated acres yields will be lower as well. So we are predicting alfalfa yield losses will be, right now on the first cutting it is 100 million plus, and if the drought continues we will lose the second cutting as well.

Other hashes, hays, brome, and fescue, are being cut now to early June, and essentially there is no hay to be cut, so I am looking at a $75 to $100 million loss right there.

The alternatives for plantings to the wheat crop are limited by the moisture availability and insect population. It would be nice if we could grow Belgian endive, but we cannot. The area where moisture is available is limited. The insect population, such as the chinch bug, limit the use of grain sorghum. In those areas as well, soybeans do not do all that well. So, the alternatives are not there.

In a sense, it is time to play "drought roulette", or "what are we going to plant if we get the soil moisture?" The old adage of do we fish or cut bait comes into play here. Most producers realize that they do not harvest a bushel if the seed stays in the bag, but they also know they lose their variable costs if they put it out there. So, it is quite a dilemma for them to go through at this particular time.

The fact of soil erosion is a scary issue and that is going to be increasing the probability if those rains do not come.

Due to current cultural practices, that is the only thing that is keeping us from another Dust Bowl condition from occurring at this moment. I feel if the culture practices were being used as they were in the 1930's we would be in the throes of a major dust bowl at the present time. But due to good soil stewardship, and situations like this where they have gone in to save fields from being blown out, it has kept us from those conditions.

The other thing that bothers me about the soil erosion aspect is due to the short amount of forage, a lot of producers will be, if they do harvest, they will be taking the straw, putting it in big bales, and then injecting with anhydrous ammonia to increase the palatability and protein content of the straw and just salvaging what they can out of this wheat crop. This leaves the soil bare to further soil erosion. Then you get into that cycle again.

Finally, you have conditions like this. This was a wheat crop that it took forever to have the crop insurance get it checked off. Over the hill from this particular field, the farmer spent a week with a bulldozer and backhoe clearing up that county road after being blown closed on that March 14 blow that we had.

Finally, we do not think about irrigated crops, which we have 3.5 million acres of irrigated crops, we do not think of the effect that a drought has on that, but it does have a very detrimental effect on it. It increases the water requirements for that irrigated crop, whether it be corn, sorghum, or soybeans.

Not to baffle you with graphics or anything, but this is, the top bar graph is the potential evapotranspiration. The bottom, the white area is the rainfall, the seasonal rainfall. So, you can consider that hatching in the center of the bar graph as the irrigation demand for the year. So this year, 1989, is probably shaping up very similar to 1988 and the 1983 cropping year in which the producers had to put on an extra amount of water.

For every extra inch of water on 3.5 million acres, that totals the per capita water use per year of Kansas, only 1 extra inch on 3.5 million acres. So you can see what this does, is it lowers the aquifer for future irrigations. This is going to push up the irrigation costs and lower profits for the irrigated producer.

Finally, being from Kansas State University I have to get this in. My department head made sure that I put this in. Agricultural research will be limited by a lack of moisture. We have one wheat breeder that has been carrying water for the past 3 weeks to his plots. He has exotic germplasm, and the material is irreplaceable. It's germplasm from all around the world. He has made crosses. If this is lost, future varieties for the Kansas farmer will be lost as well. Agricultural research is an expensive proposition. The variety of "Newton," we figure since its release in 1977 and 1978, with its improvement over the current varieties at that time has been worth nearly $700 million to this Kansas farm economy as compared to those. So we are very worried about the effect of the drought on agricultural research.

To say that we are short on grazing would be an understatement. This scene was just a few days ago and I took it because the grazed area is as short as the access area next to the interstate, so you can see the lack of growth there. Also, pond water is in short supply. So we are expecting forage losses of, at least 60 percent of normal potential. As many as 30 percent of the pastures are without livestock water. Producers are selling all or part of cow herds and transporting their cow herds across the countryside. These forage losses will be felt for 1 to 3 years.

If we get moisture, as Mike says, in the fall, we can turn around and have a decent wheat crop if weather conditions are right the next year.

The rangeland and pasturelands are not that way. It takes 1 to 3 years just to compensate, just to make up for the effect of this year's drought. So that grazing land, the—pond water that was mentioned before, and long-term management are the key to turning this around. This is where I see it is important to open CRP for grazing. It will take some pressure off of that grazing land, so that the turn-around will not be as long. It will not be that 1, 2, or 3 years, it may just be that 1 year, then the pastures will be back to normal, if the CRP can take some of the brunt of that.

Finally, local businesses. I had several county agents, 10 or 15, ask their local elevators the effect of the drought on sales and on business. We had across the State from southeast to north central to southwest, things ranged from sales are normal in the southeastern part of the State, to all the hired hands are sitting on feed sacks and watching the cirrus clouds go by.

One elevator in central Kansas estimated that their sales would be down $21 million on this year's crop and related sales would be looking at a $2.4 million net loss.

Farmers are basically keeping their hands in their pocket in this particular situation, and this is causing lots of problems with the weed populations. It is becoming severe in many areas. And that can have problems in the subsequent crops this next fall.

With that I thank you very much for allowing me to speak.

[The prepared statement of Mr. Shroyer appears at the conclusion of the hearing.]

Mr. Roberts. It is my pleasure now to introduce to you Mr. Rollie Stukenholtz who heads up Servi-Tech in Dodge City, KS, America. If Mike is the weather guru that we need at USDA, although I do not want to sentence him to that; then Rollie is the person we need at the USDA to interpret the weather and get the information out to farmers in the style and factual way he does. In regard to many of the farm publications that most of you subscribe to, they usually call Rollie first and then it appears in the farm publication. If you want to you just call Rollie first and then you do not have to go through that expense.

I do not know anybody who is more attuned to the actual conditions in farm country than Rollie Stukenholtz. He is a personal friend of mine and I am delighted he is here. One of the things I will say to my colleague Jim, I think I will introduce him—Republican. I have been waiting 10 years to do that.

STATEMENT OF ROLLIE W. STUKENHOLTZ, GENERAL MANAGER, SERVI-TECH INC.

Mr. STUKENHOLTZ. Thank you, Pat. Mr. Chairman, Dan Glickman, and Jim and Pat, ladies and gentlemen, I am Rollie Stukenholtz, general manager of Servi-Tech, a farmer-owned agricultural service organization composed of some 240 technical people that provide service for agriculture over a wide area of the Midwest.

I bring to you today a summary of the report from some 100 of our 150 field agronomists who have over the past several months been spending 6 days a week walking fields, with the exception of a few cold days in February. We have been looking at a lot of wheat across an area from Lubbock, TX, across the Oklahoma Panhandle to the eastern Colorado areas or the front slope area, far western Nebraska and the western half of Kansas.

This is the second time in the last 10 years that we have taken a poll of our people to determine the condition of a crop. The last time was in 1981 when we indicated that we thought Kansas had lost 100 million bushels of wheat because of a late freeze and we lost actually 130 million bushels.

Our report today summarizes the condition of wheat in the area that we determined has about 14 million acres planted. Based on the summary of my 24 management people, of the 14 million acres planted in the Texas/Oklahoma Panhandle across the areas I described we project that 40 percent of those acres will be abandoned. They are going to be abandoned for several reasons. In Perryton, TX for example, 80 percent of the wheat is being abandoned and this was due both to drought conditions and the Russian wheat aphid.

Areas like Dundee County, NE, 100 percent abandoned because of freeze. The area here at Barton in central Kansas, 75 to 80 percent through St. Johns will be abandoned because of dry weather conditions. And in the southwest part of Kansas which is extremely dry we will still see 40 to 45 percent of the wheat abandoned.

I talked to a USDA representative some time back and explained the situation with the irrigated wheat and he said, Why are you concerned? About moisture actually less than 10 percent of our wheat is irrigated.

Based on this 14 million acres of wheat, if we determine that that wheat would have made approximately 38 bushels, we could have harvested a crop of about 532 million bushels of wheat, worth about $1.9 billion. As a result of the drought and some of the other related causes, the dry condition along with freeze, insects, and others, we project that we will be harvesting in this 14 million acre area of wheat about 152 million bushels. This is significantly less than the Farm Bureau report this morning; significantly less than the Kansas State Board report. But this indicates that farmers from wheat alone will lose in this area of significant wheat production $1.3 billion. So regardless of how the Federal budget is sitting at this point, we will be a long way from making up the loss, Mr. Slattery.

This is the situation with wheat. In Kansas the State Board says we will harvest 9.2 million acres. We still see a significant loss, probably 30 percent of that 9.2 will be abandoned. It will be abandoned for several reasons. Now that we have had rain, it is a mixed blessing at this time of the year. We are going to see severe infestations of wheat fields. In fact the weeds are already there. At the end of next week most of the wheat fields that are living yet will take on a new color of green which will be weeds.

According to the label, the justification for treating wheat, we normally cannot treat wheat until it reaches the soft yellow stage. That means we are at least 2 weeks away from being able to start treating wheat. You cannot use—if we intend to keep the wheat for seed. That is on the label. We have areas right now that we know are already contracting wheat seed into areas that have no wheat for this fall's planting.

So we will have about 2 weeks time to spray the wheat for weeds, and if we have the wrong kind of conditions and do not get the weeds killed, we foresee the possibility of a great many more acres being abandoned. This is the problem with wheat.

The spring crop, we already have irrigated and used one-third of the total allocation according to our State water laws for the spring crop just getting it out of the ground and getting it started. In other words we have two-thirds of our water allocation left for the remainder of the season.

We have areas in eastern Colorado where they are being informed that because of only 50 percent snowfall in the mountains they may shut off the allocations from the lakes and the farmers will have their water shut off in the middle of the cropping season. This is a very critical situation. Yesterday we were informed that the Federal crop insurance people told them that if the water is shut off in the irrigation ditches, that waters much of eastern Kansas, that voids the Federal crop insurance. I would like somebody to check that one out.

Anyway, this is a significant cost and increase for us, and increase for us in production of spring crops, having to pump much more water. We already have wells in western Kansas pumping air. We already have wells that have declined in output by 25 to 30 percent due to the lowering water table.

So in terms of the cost to our irrigating producers, we can see an increase of anywhere from $20 to $40 per acre just related to the drought. That is increased pumping cost, increased amounts of water, and then another factor that came into the drought situation was the extremely poor weed control we have because herbicides do not kill weeds when it is dry. So we have had a terrible time with our herbicide problems. Areas in the State of Nebraska are a virtual disaster because of the continual weed growth.

We had labels taken from us this year such as Bladex which works very well from airplanes for post-emergence control. We can no longer use it this year.

So the impact in those areas is severe.

Our livestock producers are also being impacted by this total drought program because in western Kansas much of our backgrounding is done on wheat pastures. We have no wheat pastures to speak of this year. The irrigated wheat that was pastured all froze out so it did not pay very well in that respect.

So in terms of the impact of the drought on a significant area of the high plains, not just Kansas, we are going to see production cost increases of 25 to 30 percent. We are going to see yield reductions of irrigated crops, 50- to 70-percent reductions in dry land crops. In total impact this is going to be far more significant than the impact of the 1981 freeze which devastated many farmers, and many of those farmers are no longer farming today.

With that report, I would thank the committee for allowing me to present this testimony today.

[The prepared statement of Mr. Stukenholtz appears at the conclusion of the hearing.]

Mr. GLICKMAN. This has been one of the best panels that we have heard from ever in terms of my experience on the Agriculture Committee. The thoughtful and objective presentation of necessary information is terrific. All three of you.

I would ask first Mike Smith. I want to try to summarize in terms of short term and long term. The short term, next 60 days. Adequate precipitation in western Kansas, short east, right?

Mr. SMITH. Yes. Considering the recent rains, if we have normal precipitation the next 30 days that would probably be adequate in the western half of the State. But northeast Kansas which is actually now the worst area, since they did not get the heavy rains of the past week, normal precipitation just would not be adequate in that area.

Mr. GLICKMAN. You say if we have normal precipitation. Are you forecasting or is the National Weather Service forecasting normal precipitation?

Mr. SMITH. The National Weather Service is forecasting less than normal over eastern Kansas and normal in western Kansas. Personally, I think we are going to have near normal precipitation the next 30 days over the entire State. I think we have gone into a pattern, at least for a time, that looks much more favorable, much more like it usually is this time of year. So the extreme dryness of the past few months I think is behind us.

Mr. GLICKMAN. There has been a lot of discussion about the effects of global climatic issues. Are we in a greenhouse effect? Are we in a worldwide era of dry conditions? Much more volatile weather? And if so, it has profound implications on the farmers and ranchers. Can you comment on that?

Mr. SMITH. There is no doubt in my mind that more research is needed in this area, and there is no doubt in my mind that there is a greenhouse effect. But there is no reason to think that the greenhouse effect, which we have been able to measure in terms of the amount of carbon dioxide and other gases in the atmosphere which has been increasing for 30 years, there is no reason to think it just suddenly kicked in last spring. So I think this drought is more related to the La Nina, the water in the Pacific Ocean, than the greenhouse effect. That is not to say that the greenhouse effect will not be important some day, but this drought is more related to the La Nina.

There are indications that the La Nina is weakening and may disappear, and that is the basis for my longer term forecast meaning the end of summer, fall, being somewhat more optimistic.

Mr. GLICKMAN. A final question to Mike. I referred to it and you did as well, a little bit about the ag weather people, Dr. Streohman and others up there. Can we, and should we, rely on the accuracy of the information that USDA's weather people give us?

Mr. SMITH. It is difficult for me to comment on other meteorologists, because it is somewhat of an art, as well as a science, and different people with good intentions can see things differently. But I think there is no doubt we need a good, independent commercial weather industry, in addition to a viable Government weather industry, so there is the diversity of opinions and the objective information that legislators, farmers, and other people, need to make this sort of very important decision.

Mr. GLICKMAN. Dr. Shroyer, I would be interested to know what technique you are recommending to producers to deal with dry weather conditions. Are there things that producers could be doing to mitigate their losses? For example, I was out at Kingman County looking at some pretty bad wheat and I told the fellow there you could have planted oats on your wheat base, 100 percent if you wanted to, and not lose your wheat base, and that is a helpful thing in terms of preserving the soil and helping the soil. We talked about different strains of wheat.

Is there anything in particular out there that you can recommend to deal with periods of time when we have weather like this?

Mr. SHROYER. By my answer you might think I am running for office, but I am not really. It is going to depend. Kingman County is completely different from Johnson County, Jefferson County. Different situations whether they are livestock oriented feeders, whatever. I guess my answer is that it is going to depend so much.

Crop rotation is obviously important, and I think the point on the new farm bill would be crop substitution, excuse me. I think it is important and necessary.

As far as alternative crops, there are really none. We have sunflowers, we have summer annual forages, millet, some of those things coming on, and again, it is going to depend so much on what that producer has for other income, livestock or not.

I guess I am really not giving you a good answer, but cropping rotation is one.

Mr. GLICKMAN. Rollie, just to try to confirm your point, as I understand it, you are saying we are probably talking about a 70-percent loss when all the numbers are in in terms of the wheat crop?

Mr. STUKENHOLTZ. At this point we are projecting that 40 percent of the crop is going to be abandoned. We are estimating the remaining crop at about 15 bushels on dry land and about 40 bushels on irrigated land.

In regard to your other question, I wrote to Clayton Yeutter, back earlier about the substitution when we first recognized the wheat was gone, and asked if they could encourage the ASCS offices to release this wheat at an earlier time because there were situations that we had irrigated fields that were frozen out that could have gone for oats, or spring barley, or other crops, and the ASCS checked those fields and said: "Yes we are going to disaster them, but we will not release them for some significant period of time." This delayed the opportunity for us to substitute those crops. Consequently, nothing has been done along those lines even though I got a letter from the head ASCS person in Washington.

So we need more flexibility. When we have these disasters if we have that opportunity to get something substituted we would not be going to the—saying, Hey we want disaster payments. We would have raised a second crop and could have produced some income.

Mr. GLICKMAN. One final question, perhaps I should not be concerned with the supply of the carryovers of our Nation's wheat crop, but based upon what I am hearing here and what I heard in Texas and what I have heard from grain elevator operators, we do not have very much wheat in storage now at all in wheat country; we do not have very much wheat coming on board. I know there is some additional wheat being grown in the southeast part of the United States. Is USDA overestimating our carryover and the amount of grain that we have?

Mr. STUKENHOLTZ. In 1981 they said the freeze cost the northwest Kansas producers—they said they got 45 percent wheat crop. The elevators in that area indicated they only took in 23 percent of the normal crop. So we think there is some dispute between the USDA figures. Whether or not they are overestimated, we think right now the Kansas wheat crop is overestimated by anywhere from 40 to 70 million bushels depending on what happens after this rain. If we have to abandon several million acres because of weeds you cannot combine the wheat in weed fields, and the weeds are literally solid out there now. So we could abandon several million more acres.

Mr. SHROYER. I see the potential of another wheat streak epidemic for 1990 coming about, because of fields being abandoned. Usually, we say a wheat-streak-mosaic epidemic follows hail damage, but with the weeds there will be a lot of harvest losses, so I feel like there is probably, and I am worried about the 1990 crop already and the wheat-streak potential for that crop right now.

Mr. GLICKMAN. Thank you. Mr. Roberts.

Mr. ROBERTS. In the interest of time I am not going to ask many questions, but I want to make one observation. We in the Ag Committee, during the drought relief bill last year, authorized the substitution of very specific crops. I made the point at that time, and I know that Charlie Stenholm and I have had a substitution bill in ever since the 1985 Farm Act, based on advice by Leon Torline and the Ford County Wheat Growers, and I see Senator Don Christy out there in the audience who has been telling me this, and my predecessor, for years.

What we need to do, the Secretary now has 10 percent discretion on substitution and he has never done it because of worry about the budget. I think if we put that in and up to 20 percent, where we had it in the 1985 Farm Act, it would save money in the long run.

Dan, you have heard me make this speech many times. You made the same speech, and Jim introduced legislation. Mr. Stenholm and I have introduced a clean substitution bill to Congress just last week once again.

We have no business on the Ag Committee going crop, by crop, by crop, micromanaging farm program policy when we need to give that to the farmer.

We need to give the farmer two commodities that he desperately needs in regard to substitution as evidenced by the testimony and that is consistency and predictability and get this substitution in the 1990 farm bill. With that observation, in the interest of time, I will yield back.

I would just make an observation and I have argued this around the Budget Committee that in fact if we use substitution we will save the taxpayers money. I am absolutely convinced of that.

Mr. SLATTERY. What can be done about wheat streak? You referred to that and I just want to take a second. What can be done as we look into the 1990 years?

Mr. SHROYER. There are several things. No one should plant wheat, I suppose that would be one——

[Laughter.]

But since that is not feasible, we will go to the second one.

There are several varieties that show some tolerance to the wheat curl mite, which is the vector that carries the disease. And those varieties have shown up in the past couple of years doing well in this region.

The other thing is good soil stewardship, good neighbor policy, getting rid of all the volunteer wheat, since volunteer wheat is what harbors the wheat curl mite. If you do not control the volunteer and you plant too soon before the volunteer is destroyed, or if it was just destroyed, the wheat curl mite just migrates over into your new crop and infects it at that time.

Mr. SLATTERY. Let me ask you just a follow up. Is this a serious enough problem that we should try to create some kind of incentive in the law dealing with disaster assistance to encourage people to destroy the volunteers?

Mr. SHROYER. I definitely think so.

Mr. SLATTERY. That is an interesting point. Thank you very much.

Mr. GLICKMAN. Thank you all. Excellent testimony today. I appreciate it.

Our next panel is a group of Kansas basically farm organizations. Mr. Bob Paris, president of the Kansas Association of Wheat Growers; Mr. Donald Lundquist, treasurer and former president of Kansas Corn Growers; Mr. Thomas Tunnel, executive director, Kansas Grain and Feed Association; Mr. Dana Hauck, former chairman of the Cow/Calf Stocker Council, Kansas Livestock Association; and Mr. Elmer Davis, president of the Kansas Soybean Association.

We appreciate this panel here. I am sorry it has taken so long, but I think it has been very productive. I think most of you have written statements.

I might mention for the record that all your statements will appear in the record so if you want to read them that is fine, if you want to summarize them, that is fine, but they will appear in the record.

I would also mention to the audience, if any of you have statements you want to be included in the record, after the hearing is over bring them up to the staff back here and they will be included in the record as well. We will leave the record open for 1 week if anybody else wants to include their statements for the record.

Why don't we go ahead and begin, and let's do it as your names appear on the list. So Bob, we will start with you.

STATEMENT OF ROBERT A. PARIS, PRESIDENT, KANSAS ASSOCIATION OF WHEAT GROWERS

Mr. PARIS. Thank you Mr. Chairman, and members of the subcommittee. I am president of the Kansas Association of Wheat Growers. I appreciate this opportunity to give a presentation here today.

I think we have heard enough about the doom and gloom of the drought. I will not read my written testimony that I have given the committee. I would like to make some comments.

I take it, Mr. Chairman, that we are here today for solutions and maybe just not all commentaries. I would like to direct my thoughts here today to some of those thoughts.

As you know we had all the problems with the wheat, of getting it in and getting it through the winter, and all these things. We already know that. We have experienced those. We have heard a lot of testimony and will probably hear more today. If you had been here March 14 as compared to last week's weather you would realize this is a meteorological battleground of the United States here in the Great Plains. I live 100 miles straight west of here and we could not see our house from our shop. It was pretty bad.

So we know some of those things and we have lived around it long enough to see it. I have pictures of the dust storms in 1935 of April 14 which was the great Dust Bowl days. I have some pictures of those.

My comments today, I would like to talk about crop insurance, and I would like to talk about the normal crop acres, and also the seed wheat situation as the three major topics.

In a written testimony, I stated that possibly the farmer-owned reserve might be a potential of some seed wheat coming out as one source. I heard a salesman the other day telling me that his wheat, last year, sold for $6 and now he went up to $9.50 and in 2 weeks I am going to raise it to $11.50 a bushel. So the seed wheat thing could be a problem this fall for many producers. I mention that as something to be thinking about from the producers' standpoint.

On the crop insurance issue, some of that is in my testimony. But I think at present I have carried crop insurance for 4 or 5 years. It does not seem to me like, as I study the variable costs and the fixed cost of my operation, that at best, it only covers part of the variable cost, and by the time you need drought assistance or crop insurance, you have managed to increase your variable costs considerably because you are going to look at some alternate situations. So I think we need a crop insurance program that would address these things in a little different way.

The capital intensity of farming today is getting greater all the time. I think we will hear some testimony before the day is over that our variable costs have probably risen, since the 1985 Farm Security Act, some $20 an acre. Yet our target price is looking at maybe coming down some. So I think to protect farm income we need to look at this situation pretty strong.

My experience with crop insurance, with grain sorghum, has been kind of this way. We have had some terrible hot summers. Here I paid the full premium and my yields were just exactly on the borderline for insurance and I had to pay the full premium and here I had a disaster and got no relief, and I think that is typical.

I agree with Secretary Yeutter on the subject that if we cannot make this crop insurance thing work, let's junk it. I think that is where it is going.

So I would like to propose some thoughts for the crop insurance in the future. What we need is a program similar to hail or fire insurance to protect that dollar amount that is invested in those acres. If I had a $50 variable cost in my farm and $25 fixed cost that I would have obligated to the banker on a loan, I should be able to protect that loan with a crop insurance program, and we would not need this disaster relief if we had this type of program.

You can do these things with fire insurance or hail insurance. You can get at a level $50 or $75 or $100 an acre to cover those costs, but we do not have that with the present crop insurance program the way I read it. There are so many different ways of signing up. If we could keep it simple, if we could it—not have 27 ways to sign up. I do not like that confusion.

I think we need to keep the cost of the program somewhere in the 5-percent level, maybe of what those crop costs are or what you are insuring for for a fee. So just a roughout of that, if you had $50 variable cost, maybe we could pay a $5 premium and $7 for $70, I don't know. I don't know where the actuarial part of that would come out, but that is a start maybe to look at.

The Government's role in this is farmer participation, of course. We need to attract farmers in it. Whether to make it mandatory or not, I have reservations on anything mandatory. But to make the crop insurance program work on a national scale it might have to be looked at.

I hate to keep running to the Federal Government all the time to say gee, we need disaster relief. I would like to have a program that would work so we do not have to do those kinds of things.

I think bankers would really appreciate this kind of approach because they would have a way they could protect that loan. I could come in and say after the 1981 wheat freeze I really got my farm in a bind because I lost my entire production. My cost of production that year was $15,000 a bushel. I cannot afford many of those. Crop insurance became important in my farming operation because of that 1981 drought and I am still trying to get out of that.

Another thing along with crop insurance, I think it would stabilize rural America really well, because these small towns are not going to be dependent upon anything but you farmers and us in agriculture because we do not have transportation in and out of our town, we do not have the labor force, we do not have the water. So crop insurance could stabilize some of these rural communities and that would give a lesser cost to the Government.

I think the best decision we could make today is not to get the set-aside down to zero. I know we need to produce back to normal, but if we have a good crop next year we can bury ourselves with commodities and prices again would be right back where we were with the previous farm program, and that is a personal opinion on my own part about getting the set-aside to zero, but I think we need to keep it at the present level for the present time to get out of this. I would hate to see it go down to zero.

The other thing is, and I will quit this, the drought got so bad here I was kind of worried about my own wheat, and I quit grazing the Russian wheat aphids.

Anyway, the normal crop acre concept that we had for wheat and the wheat growers in the State of Kansas has been pushing for this ever since it was eliminated. Bill Leisher and I got in a contest one time about the subject of normal crop acres and he won. But anyway, it is one of the best tools we have to manage drought conditions in the Great Plains. Good water management starts with good land management, and we cannot have good land management without flexibility in planting the crops in the State of Kansas.

Subsoil moisture is what makes this State fly and we have to work on land management progress. I am a conservation nut and I live out there where an inch of moisture is very valuable, as it is to all of you. But the normal crop acre concept, that is, one, manage that subsoil in a crop rotation that helps minimize the dry weather effect.

With that I guess, Mr. Chairman, I will conclude my remarks.

[The prepared statement of Mr. Paris appears at the conclusion of the hearing.]

Mr. GLICKMAN. I appreciate your testimony, Bob, and also appreciate the input of the Kansas Wheat Growers generally.

Next, Mr. Lundquist.

STATEMENT OF DONALD LUNDQUIST, TREASURER AND FORMER PRESIDENT, KANSAS CORN GROWERS ASSOCIATION

Mr. LUNDQUIST. Chairman Glickman and distinguished committee members. Thank you for the opportunity to appear before you today, and thank you for coming back to Kansas to assess our needs in this critical situation.

I am Don Lundquist, currently treasurer and immediate past president of the Kansas Corn Growers Association. I have been a producer of corn, soybeans, wheat, milo, alfalfa, and feeder cattle for the past 35 years in the Smoky Hill River Valley of central Kansas near Lindsborg, KS.

Although Kansas is rarely thought of as a major corn producing State, the 1988 corn production ranked eighth in the volume of bushels produced in the United States. The 1988 production in Kansas was 143.75 million bushels with a dollar value of $395 million.

Kansas corn producers in 1988 planted 1.2 million acres with approximately 100,000 acres of that being utilized for silage. Seventy-five percent of the total acres are irrigated and the other 25 percent is in dryland production. Nearly all the dryland acres are in the easter third of the State where the drought is in its second year.

Nationally, about 50 percent of the corn harvested is fed to livestock and poultry. In Kansas that percentage is higher due to the volume of corn used by the feedlot industry.

As of May 14, 1989, 85 percent of the Kansas corn crop had been planted, according to the Kansas Department of Ag Statistics. In my immediate area the figure is closer to 50 percent due to the extreme drought conditions leaving no moisture in the seed bed. The 1.5-inch rain that we received this week was the first one over 1-inch measurement since October 5, 1988, along with no snow during the winter.

As I mentioned earlier, I have been a diversified producer for the past 35 years. I have learned during those years that all commodities are dependent upon each other, that is, if one crop was bad, we had a chance to make it up with an above average yield from another. This year I believe that our chances for this happening are very slim. The wheat and livestock segments are already in a critical stage. The first crop of alfalfa is practically nonexistent. I am sure you are aware that 95 of the 105 Kansas counties have been approved for the livestock drought assistance programs. Feed grains and soybeans this summer will have to have above average rainfall to make up for the deficiency in subsoil moisture.

Irrigators are also not exempt from drought conditions. Those pumping from rivers and streams are faced with extremely low water supplies. Ground water levels are lower due to insufficient recharge. Some producers have used up much of their water allocation just in preirrigating. All of this adds much to the production costs of the crop and results in less, if any, profit.

The points that I have been making bring the conclusion, that the Kansas Corn Growers Association request that any legislation to extend the 1988 Disaster Assistance Act, would include 1989 spring planted feed grains and soybeans along with 1988 planted wheat.

Thank you again for the opportunity to appear here today, and I will be glad to answer any questions.

[The prepared statement of Mr. Lundquist appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much, Mr. Lundquist.

Tom, it is a pleasure to have you here today.

STATEMENT OF THOMAS R. TUNNELL, EXECUTIVE VICE PRESIDENT, KANSAS GRAIN AND FEED ASSOCIATION

Mr. TUNNELL. Thank you, Chairman Glickman, Congressman Roberts, and Congressman Slattery.

I am Tom R. Tunnell, executive vice president of the Kansas Grain and Feed Association. The organization I represent here today is a voluntary trade association having approximately 900 members, including Kansas grain and feed firms ranging in size from the smallest locally owned country elevator up to the largest terminal elevator. Ownership of our member firms is about equally divided between farmer-owned cooperatives and independently held grain companies.

You have already heard today about the devastating effect the drought is having on Kansas agriculture. Loosely quoting an old Chinese proverb, "All boats in a harbor will rise and fall with the same tide." Such is the case with Kansas agriculture in that a reduced wheat crop and a resultant loss of income to Kansas farmers will have a major impact on Kansas agribusiness and principally Kansas grain elevators.

Going into the drought in late 1988, Kansas elevators were already in a weakened state because of a massive liquidation of Commodity Credit Corporation owned wheat and feed grain stocks. This caused a tremendous reduction in storage income to our members. As a result of this liquidation, grain in storage in commercial warehouses across the State now averages approximately 20 percent of total storage capacity. With the prediction of under a 200 million bushel wheat crop, which most people as you have heard today is optimistic, prospects are certainly dismal in terms of potential income to our elevators for this crop year.

Attached to my testimony are several letters from KGFA members which describe the impact of the drought in their respective geographic areas. For illustration purposes, let me briefly review the information provided by one, Northcentral Kansas Cooperative, Farmway Co-Op in Beloit.

They predict as a result of the drought that they will see a reduction in wheat sales of $21 million which will have a resulting reduction in their margin income, gross income, of $660,000. In milo they see a $2 million loss in milo sales, a margin reduction of $176,000. Other grains they see a $300,000 reduction in sales for a margin reduction of $23,000. This equals $859,000 for this crop year in terms of margin reduction. When you add to that storage and handling income loss of $341,000, and they are predicting a $1.2 million loss this year just in potential grain handling income.

In terms of other operations, they are seeing a total, including feed sales, fertilizer sales, and chemical sales, they are seeing a total reduction of $1.2 million for a projected loss in 1989–90 of $2.4 million.

This year the expected wheat harvest will be the worst in 25 years. Even with the recent rain the fall crop will also be below normal. The subsoil moisture profile is just not adequate to grow fall crops without additional quantities of rain to rebuild it. If the drought does not let up soon, then most farmers will most likely participate in 0/92 programs, and thus we'll see minimal fall harvest bushels hauled to grain elevators across our State.

In preparation for my remarks, Mr. Chairman, we held a conference call of our executive committee made up of seven grain men, members of our board of directors from across the State, and asked for ideas on possible suggestions we could make to the subcommittee. The consensus of this group was to be supportive of legislation which you have already introduced to extend the 1988 Disaster Assistance Act to cover all crops planted in 1988 for harvest in 1989, as well as the perennials you have already mentioned, and the feed grain that will be planted this spring.

Further, our association would favor any legislation that would provide immediate financial assistance to farmers and ranchers, especially in the area of emergency feed assistance. In this vein our association recommends a moratorium be placed immediately on all future sales of all Kansas stored Commodity Credit Corporation cataloged stocks until such time as it can be determined how much of this grain may be needed for emergency feed use. It makes no sense to move CCC stocks out of Kansas at this time only to turn around and buy it back later for possible emergency feed use.

You asked, Congressman Glickman, about CCC stocks for the State. I contacted the Kansas City Commodity Office and in my testimony, which you may not have before you, they informed me that current Commodity Credit owned, catalogued and noncataloged stocks in terms of wheat, there is 37.7 million bushels in the State of Commodity Credit owned stocks. In the farmer-owned reserve they have 15.9 million bushels of wheat. In the regular loan program there is 1.2 million bushels of wheat. I also have the corn and milo figures there.

If you put that in perspective, in that we have 900 million bushels of commercially licensed storage in the State, and about 400 million bushels of farm storage, we barely have the bin bottoms covered with what is left over in our State right now.

In closing, our industry has not asked today for direct Government assistance for the grain and feed industry except the minimal continuation of Government storage income if the moratorium is placed on the sale of CCC stocks in Kansas. Again, it is our position to be supportive of immediate drought relief for farmers and ranchers.

Thank you.

[The prepared statement of Mr. Tunnell appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you, Mr. Tunnell. Dana, it is a pleasure to have you.

STATEMENT OF DANA R. HAUCK, FORMER CHAIRMAN, COW-CALF/STOCKER COUNCIL, KANSAS LIVESTOCK ASSOCIATION

Mr. HAUCK. Thank you, Mr. Chairman.

On behalf of the Kansas Livestock Association, I want to thank you for allowing us to comment about the drought's effect on Kansas farmers and ranchers, and more specifically, the Kansas livestock industry. I realize that your subcommittee does not handle livestock matters, but we are a major consumer of feed grains.

Last year Kansas feedyards fed 4.15 million cattle and used over 180 million bushels of grain, 8 million bushels of soybeans, and 8 billion pounds of silage and hay. These figures do not include the grain and forage fed to our cowherds and stocker cattle. My comments today offer suggestions for possible drought legislation plus highlight our concerns with USDA.

This spring's drought condition is merely an extension of the dry weather we faced in 1988 in my area and most areas of the State. We have used virtually all stocks of hay and other forage sources. We were awaiting the green pastures that normally occur in mid-April. However, as you travel the State, you will find little, if any, grazing available for cowherds and stocker operators. Ponds are very low or completely dried up. We have seen the depletion of many of our stock watering wells and springs, and we are virtually in a panic situation. I would like to summarize some data which verifies that the drought has caused cowherd liquidation and/or movement and a change in feeder cattle programs.

Much of this does appear in the written testimony so I will be somewhat brief.

As Secretary Brownback indicated, the Kansas lab is presently receiving 4,000 to 8,000 blood samples per day. Normally during April they would receive only about 2,500 samples a day. Kansas cow slaughter is four times as large as it was last year. The latest USDA shows that 25,000 to 29,000 cows were killed on a weekly basis during the last half of April in Kansas, Nebraska, Missouri, and Iowa. This represents nearly a 40-percent increase in cow slaughter.

I might mention that this is occurring at a time when our cowherd numbers have been under liquidation for a number of years and are the lowest at any time since 1952.

Feeder cattle operations are also being affected. Because of the grass situation, many cattle are moved to feed yards at a much earlier date and this trend will likely continue. Placements in Kansas feed yards reflect this movement. April was a record setting month for placements with 370,000 head. In fact, the first 4 months set a record for Kansas feed yard placements. All of this has happened when we supposedly have 8 million fewer feeder cattle than what we had in 1982.

The Kansas Livestock Association is pleased that USDA has allowed haying and grazing of Acreage Conservation Reserve and Conserving Use acres for most Kansas counties. However, if we fail to receive timely rains for the rest of the growing season, our producers will probably be unable to grow or harvest any feed supplies on this acreage. So the verdict is still out on whether this haying and grazing of ACR and CU will really benefit the livestock industry. Nonetheless, we do appreciate USDA attention on this issue.

We have instituted a self-help program. At the NCA board meeting in Washington, KLA suggested that cattlemen in more fortunate geographic areas across the country might open their grazing for cowherd operators in this part of the country who desperately need to relocate their herds. NCA has implemented what we are calling the Cattlemen's Forage Clearinghouse in an attempt to list individuals who have grass in other geographic areas so that cattlemen can reach these other people and contact them for potential grazing agreements.

As of Tuesday, May 16, the NCA office in Denver had received 150 calls from people looking for grass, 90 percent of which were from Kansas, while only 49 people had called listing grass available. Most of these were in Oregon, Idaho, and other Western States.

I might also add that the Kansas Board of Agriculture's forage hotline is working in conjunction with the NCA program and has received nearly 800 calls with most of those people seeking pasture or hay.

Our association has also identified several other areas that USDA can be of help to temper the impact of drought for cattlemen. On May 4, KLA sent a letter to USDA asking the Department to implement three programs that they have the authority to activate. The first of these which has had some discussion this morning is the haying and grazing of CRP acres. To date, we have never in the past suggested using these acres, but due to the emergency situation we feel it would be appropriate to open up this land for livestock feeding purposes.

I might comment that we feel that this land should be opened up to grazing as well as haying. In some cases, I firmly believe there would actually be less damage from grazing than haying. At the same time, there is often water available in some of the draws and waterways and often ponds in some of these areas that would be able to be utilized under grazing when they would not be under haying alone.

The second thing we recommended was cost share on water projects. Last year's drought bill gave USDA the authority to cost share on expenses incurred for water projects. Since last summer many cattlemen have in fact drilled new wells, worked on abandoned wells, installed many miles of pipelines, developed springs, renovated windmills, and performed much needed construction work on ponds. These activities amounted to significant emergency expense, and we strongly feel that USDA should implement this program and it should be retroactive to last spring, 1 year ago.

The third thing we recommended was in regard to the livestock transportation program. This provision was also a part of last year's drought bill, as you are aware. I will not go into this in great detail. I would say that it would be a big benefit to many cattle owners who have already shipped their cowherds to several States away and I am sure that many more operators are looking for this alternative but may not find it economically feasible without some cost assistance in transportation.

And on this matter we would suggest that this cost share be provided for two-way transportation so the cowherds will be moved back to our State and help our local economies. We are willing to limit this cost-share program to transportation for foundation cowherd stock only.

Again, I must emphasize, these two cost-share provisions will be basically meaningless if they are implemented without being retroactive. Many cows have already been moved or sold, water expenses have already been incurred, yearlings are moving to feed yards, and feed assistance was needed prior to May 1.

When discussing these proposals with fellow cattlemen they express doubt and say that in all likelihood there will be too little too late.

Mr. Chairman, these three proposals have been sent to USDA. To date, we have not received word or even a note of confirmation from our letter. You and your committee may be helpful in encouraging the Department to move in a more expeditious manner. We do not feel we are asking for too much in order to save our cowherds or make long term financial decisions. We cannot wait much longer for word from the Department of Agriculture. If they are not going to implement the programs, I wish they would let us know.

I think you can appreciate how angry cattlemen will be if these programs are announced and implemented when it is too late. Our producers are currently operating day to day and we need faster action from USDA.

KLA's cow-calf/stocker council executive committee met this past Thursday and we spent considerable time discussing the role Government could play in minimizing the drought's impact. We arrived at two additional suggestions that will likely take congressional action to implement.

Section 1033 of the Tax Code allows for a special treatment of income received from the sale of breeding livestock sold because of drought. This rule applies to money received from the sale of breeding stock, or in other words those subject to capital gains in excess of the normal culling rate of your operation. This law allows producers 2 years to reinvest money in a breeding herd. We would ask that this 2-year period be extended to a 4-year period. It is not always easy to relocate breeding herd replacements that fit each individual operation or have comparable genetics to the ones that have been liquidated.

Our committee discussed at great length the problems with the two livestock feed programs. No doubt these are helping some producers. However, the programs are no more than a faulty crutch to many. These two feed programs provide cost-share assistance or CCC grain at a discount price for livestock owners who face a 40-percent or more loss in feed production. Our producers are being told the feeding period, in other words the time used to calculate the feed needs, ends when the next source of feed is available. In other words, those producers who will be harvesting their first cutting of alfalfa very shortly may apply for a time period only from May 1 until the very present time.

I want to point out that this feed is ordinarily used for winter feed. There is no way that a cow/calf producer can plan his feed program if he has to reapply every 2 weeks.

The other complaint was that the use of feed on hand is a detriment for calculating eligibility. The more a producer scrimps and plans, the less assistance he or she receives. These programs penalize prudent managers. If we are going to have feed assistance programs let's make them fairer and simpler. Why not simply provide assistance for a producer's loss and not penalize someone who may have feed on hand or grow a supply of feed for use this winter. Perhaps we should redirect the feed program through legislation. Our association stands willing to work for more practical and useful livestock feeding programs.

I would again like to thank you for your interest and support, and I hope we can work together to minimize the drought's impact to the livestock industry.

[The prepared statement of Mr. Hauck appears at the conclusion of the hearing.]

Mr. Glickman. Thank you, Mr. Hauck.

Elmer, it is a pleasure to have you here today on behalf of the Soybean Growers Association. You may proceed.

STATEMENT OF ELMER E. DAVIS, PRESIDENT, KANSAS SOYBEAN ASSOCIATION

Mr. Davis. Thank you. It is a pleasure to be here today. I am Elmer Davis, president of the Kansas Soybean Association. I am a farmer from Haviland, KS where I produce soybeans, wheat, and corn.

Soybeans are an important cash crop in Kansas. In 1987 the last normal year, Kansas farmers planted over 2 million acres of soybeans and harvested over 67 million bushels. In today's market this normal size crop would mean about $470 million in farm income for Kansas.

Mr. Chairman, Mr. Roberts, Mr. Slattery, thank you for coming to the country to hear from farmers and others directly affected by the important decisions you will make.

Before addressing the serious drought outlook for soybeans in Kansas, I want to thank Chairman Glickman for his leadership in important agricultural issues in general and on soybeans in particular. We greatly appreciate your efforts, and Mr. Roberts' and several others of this distinguished subcommittee, to give farmers more freedom to make planting decisions for the market based on what is best for their own farming operation. Increased planting flexibility is good policy and we support it.

Mr. Chairman, Kansas soybean farmers also strongly support legislation you jointly sponsored with Congressman Marlenee with the support of other Members of Congress to establish a nationwide soybean promotion and research program. Farmers would control the program at the State and national level. This self-help program would allow farmers across the country to work together to increase soybean profits.

For example, we hope to invest funds to develop more drought resistant soybeans with improved plant water utilization and better pest/disease resistance.

The drought in Kansas this year may well affect the outlook for spring-planted crops such as soybeans, especially in eastern and central parts of the State where drought has been the worst. Subsoil moisture and water levels are low with little, if any, reserve. The rain earlier this week was the first significant rain we have had since March, and many parts of the State did not even get the March rain. Unless we continue to get needed moisture, Kansas soybean production will be critically low this summer.

I would like to add parenthetically here that I had an opportunity to visit with some other KSA board members just yesterday after the rains of this week, and at this point their estimate, even if we were to have an average rainfall for the summer, they would be looking at somewhere from half to two-thirds of a crop because of the lack of any subsoil moisture. So the drought is not over by any means.

Not only will it be hard for Kansas farmers to make a crop, but drought also means lower yields, pesticide carryover problems, and more pests and disease in the dry period.

Drought also has serious implications for irrigated soybeans grown mainly in western Kansas. Irrigated soybeans have been drawing heavily on the Ogalalla aquifer. On my farm we have had to irrigate several times already, which is very unusual. I fear such practices will have serious long-term consequences for this important water resource. But farmers have little alternative if we are to produce a crop and make a living.

As you consider drought legislation we urge you to include financial assistance for soybean farmers who indeed suffer eligible losses. The Disaster Assistance Act of 1989 (H.R. 2232) accomplishes this objective.

We support the bill's disaster payment provision, but suggest an improvement would be to allow farmers to determine losses based on their proven soybean yield rather than a State, area, or county yield as provided in the bill. Use of proven yield would reflect actual production, not just average production.

If soybean farmers could use a proven yield to calculate losses, then drought assistance triggered at the 35- to 75-percent crop loss levels would more closely reflect the actual percentage of the crop lost.

Regarding crop insurance, we support the provision in H.R. 2232 which extends crop insurance sign-up until at least July 1, 1989. This will allow farmers to voluntarily choose whether to enroll in crop insurance, depending on the crop outlook.

Soybean farmers support congressional efforts to encourage voluntary participation in the Federal crop insurance program as a positive risk management tool.

Finally, based on experience with implementation of last year's drought bill, we recommend that H.R. 2232 be modified to require USDA to offer crop quality reduction disaster payments based on the criteria of the bill. Last year certain regions of the country suffered significant drought-induced crop quality problems; for example, shriveled, wrinkled soybeans, shattering from low moisture, and damage from spider mites, et cetera. USDA declined to offer additional payments for these drought-caused quality problems. Affected soybean producers faced severe price discounts and in some cases purchase refusals due to drought damage. A simple change of one word, from "may" to "shall" would solve this problem.

Mr. Chairman, that concludes my remarks. Thank you very much.

[The prepared statement of Mr. Davis appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much. All the statements were particularly useful to us.

Tom, I just want to followup on a question I asked you before. You gave us some pretty bleak numbers in terms of the amount of grain in storage and that is obviously going to affect your members rather dramatically. Does your national organization have any numbers on total grain and whether the USDA figures are accurate on carryover?

Mr. TUNNELL. I am sure they have those numbers. I am not sure whether we compared them to what USDA has put out, but I would be happy to do that. I think that would be very good information to have.

Mr. GLICKMAN. What you are basically telling us is that if on the farm there is none there, and in storage there is none there, then we do not have any grain in Kansas.

Mr. TUNNELL. Based on the numbers I received yesterday from the Kansas City Commodity Office, we have about 60 million bushels of wheat on hand in the State, which is pretty low.

Mr. GLICKMAN. That is wheat and feed grain?

Mr. TUNNELL. Well wheat, 37.7 CCC owned, 15.9 farmer owned, and 1.2 in regular. As far as corn, CCC owns about 20 million bushel. In terms of grain sorghum, about 65 million hundredweight.

Mr. GLICKMAN. That compares to let's say what we would have been last year and the year before.

Mr. TUNNELL. I know last year, going into wheat harvest, we were about 65 to 70 percent filled, as I recall, and we were concerned about railcar availability and making space for harvest. Now I think, without a doubt, we can hold this wheat crop and maybe two or three more.

Mr. GLICKMAN. Are they still doing this catalog thing?

Mr. TUNNELL. Yes they are. We are still into the grain now, we still have EDP. We are not proposing that we do away with the—enhancement program, excuse me Congressman Roberts. I did not mean to bring that up. But if we could have a moratorium for awhile on catalog grain and keep this grain from being moved out of our elevators it would certainly help our storage income. But also we would like to think it would be available, if we need it, for emergency feed use.

Mr. GLICKMAN. Also, Mr. Davis, quality reduction. You talked about crop quality reduction. Last year's bill did provide, didn't it, some participation in the program for quality reduction?

Mr. DAVIS. It said "may," but the Secretary——

Mr. GLICKMAN. So the Department did not implement that at all?

Mr. DAVIS. That is my understanding. I don't know if that was every case, but that was certainly what we found. This was primarily in the South, I believe, where they had these particular problems. They chose to decide that they were not worthy of pay.

Mr. GLICKMAN. That is something I want to look at further because I know that—I think it was Pat who got language in the bill last year—that had the drought-related so that we could get mosaic and stuff like that, that may have not resulted in a complete loss. I do not know if that is categorized as quality reduction or complete loss or whatever, but I appreciate your comments on that. Thank you.

Mr. ROBERTS. I just have a comment in regard to your testimony, Dana. I thank you for your testimony.

The gentleman who has the letter sent—by the Kansas Livestock Association—by Warren Weaver who is your president, is a guy named Geik. He is in Washington with the USDA. I hand delivered it to him.

Now it went to Dick Crowder who is the chairman of the drought task force that appeared before our subcommittee several weeks ago. Because you have not received an interim reply, that is, "Dear Warren, Thank you for your letter. We are from the government and we are here to help," does not mean that they are not now considering that response. The basic reason why they have not responded, and I do not mean to take up the subcommittee's time on this one complaint again, or to split the shingle, is because of, quite frankly, the security checks and the White House personnel policy that has led to a situation where Government has almost been stymied because of the new yardsticks we are now setting for appointments and for service in Washington.

We now have a situation, because of circumstances, obvious circumstances in Washington, where you have to be a celibate monk before you can serve in any capacity in one of the alphabet soup agencies we have there, and we cannot get any answers. [Laughter.]

Now we have answers. As of next week I have indicated earlier, there will be some water—money for our ponds and our—let us not say hay and grazing any more. Let's put it grazing and haying if we can. I do not know about transportation assistance. They indicated they had that in the drought bill last year. It is awkward and there is a lot of chance for fraud and abuse and it is very very difficult. But Senator Kassebaum and Senator Dole have that in their bill, they mandate it. So we will see what happens with that.

With the grazing situation, we have told the environmental groups who have already indicated to the Secretary they are very strongly opposed. It is like the conservation compliance problems that we had. Again, I would hope that the, what I would label the more radical environmental groups do not become adversaries to a real crisis management tool. They can overreact. We mow this, we burn it. If they are worried about the little critters who are endangered in there we can either burn them or cut them or we can turn the cows loose on them. I have never seen an endangered species yet that came out the back end of a cow.

So we are going to keep pushing on the grazing side, but it is going to be a tough hurdle, and I would anticipate that if the KLA asks for three and we got two, in Washington that is a pretty good average.

Mr. SLATTERY. As usual, Mr. Roberts is always a tough act to follow. What was that line? "Endangered species coming out of the back end of a cow." That has to be the quote of the day.

Mr. TUNNELL. It is my understanding he goes and looks periodically. [Laughter.]

Mr. SLATTERY. Dana, I want you to know that after I received your letter on, I think it was dated May 4, I fired off a letter to the Secretary of Agriculture on May 8, basically urging him to respond favorably to your request on haying and grazing and emergency livestock transportation assistance, and also on the provisions of the emergency conservation program dealing with the livestock water situation.

I would just observe—I am sitting here today and sharing with Dan Glickman that my family has been farming in Kansas now for more than 130 years. My father did not like to look to the Federal

Government. Every time I pick up the phone to talk to my brother, about how things are out on the farm, I get a good earful of the most recent mistakes the Federal Government has made as it affects agriculture.

As I sit here today Dana, I can't think of any other instance when the Kansas Livestock Association in the time I have been involved in Government service has ever approached us in Washington and asked us for anything. That is one of the reasons I responded so quickly to your letter.

When I was listening to Mr. Paris talk about this crop insurance thing, I just want you to know that I want to work with you and other commodity groups here in Kansas in trying to fashion, I think all of us do, a crop insurance program that is sensible and workable so that in the future we do not have to have Kansas farmers coming to the Federal Government, asking the Federal Government for assistance. My dad did not want to do that, my brother does not like to do it, and I do not think there is a person in this room that enjoys doing it.

I think one of the things we can do, perhaps the most important thing we can do, and I realize it does not necessarily deal with the livestock problems that we have, but certainly for commodity programs it does, and that is to come up with a crop insurance program that is workable, affordable, and eliminates the need for us having to have these kind of emergency programs in the future.

So for all of you commodity groups here in Kansas I would really urge you to get together and come to us with a consensus package of ideas as to what can be done. I know that some of you are working on that now. But I see that as something we can do that is very important and will help the farmers, help the taxpayers, and help everybody involved in this whole issue.

Tom, I wanted to ask a question, if I could, on this storage of grain. Tell me a little bit more about how much feed grains we currently have in storage here in Kansas compared to what we normally have. I guess my question is this, Are we going to get into a situation here in the not too distant future where we are going to run out of grain here in Kansas to feed cattle in Kansas? That is my question. Do you have any information that can shed some light on that?

Mr. TUNNELL. Just the numbers I quoted previously, Congressman.

Mr. SLATTERY. How do those compare numerically with previous years? Do you know?

Mr. TUNNELL. I don't have those comparisons, I am sorry.

Mr. SLATTERY. Can you find those for me?

Mr. TUNNELL. I sure can.

Mr. SLATTERY. I am sitting here, and this always makes my staff very nervous when I do this, but I am going to sort of think out loud with you for a second. I am sitting here thinking that I am concerned that we are going to make some agreements with the Soviet Union, and if they are not careful they are going to buy some pretty cheap wheat, and about 1 year from now or maybe 18 months from now we are going to be in a situation where the wheat that they are taking delivery on perhaps then is going to look awful, awful cheap, and we are going to be in a situation where we are going to be subsidizing the sale of wheat to them and then buying wheat in this country that may cost a whole lot more here. I do not know how in the world we can deal with that, but I would sure like to hear any ideas you might have.

It seems to me that in the past we have gone through some situations where the Russians maybe knew more about what was going on with our wheat and grain storage situation in this country than the Kansas farmers did. That is a source of deep concern with me. I am just sort of thinking out loud with you, but I would like to hear any thoughts you might have on what we can do to prevent that sort of thing from developing here in the future.

Mr. TUNNELL. I think we need to get an accurate accounting of just what our position is. I think Congressman Glickman has a very valid point. We need to know. Certainly in light of this drought we have a tendency to live in a fishbowl. I have heard that we are looking to the second largest carryover of wheat worldwide that we have ever had, but certainly in this part of the country if we export at all we may need it back. I think you have a very valid point.

Mr. SLATTERY. I read these reports dealing with the total volume of wheat but what it does not tell us, unless you really get into it, is the types of wheat involved.

Mr. PARIS. Congressman Slattery, my statement about zero set-aside is very important in what you are asking there. If we are going to keep the export enhancement and deal with these countries, I think it would be all right to go zero set-aside. But if we are going to limit the export enhancement, we just came through the most dramatic reduction in stocks we have seen in the last 2 or 3 years, and here the drought is compounding the issue. But I think if we want to keep a farm price out here we have to manage that really carefully. That is my statement from our position.

Mr. SLATTERY. No further questions.

Mr. GLICKMAN. I want to thank this panel for excellent testimony.

The next panel is Mr. Jim Rice, States spokesman, American Agriculture Movement, Liberal, KS; Mr. Dennis Shirley, vice chairman, Wichita District, Farm Credit Council and Farm Credit Bank of Wichita; Ms. Pam Dietz, member and producer of Kansas Farm Bureau; Mr. Paul Bower, National Farmers' Organization, Jennings, KS; and Mr. Tom Giessel, vice president, Kansas Farmers Union, Larned, KS.

Mr. Leroy Bower is filling in for Mr. Paul Nauer. That is pretty clever, to get names that rhyme.

We appreciate you all coming down here today. You may proceed at your own pleasure. If you have written statements they will appear in the record in their entirety.

STATEMENT OF JIMMIE R. RICE, KANSAS STATE PRESIDENT AMERICAN AGRICULTURE MOVEMENT, INC.

Mr. RICE. Thank you, Mr. Chairman, Mr. Slattery, and wherever Brother Pat went. I appreciate the opportunity and also thank you for inviting me to explain the situation as I see it here in the State.

I am Jim Rice. I am a farmer in Seward County, Kansas, and I also represent the American Agriculture Movement, Inc., serving as Kansas president of that organization presently. We operate a family farm operation in southwest Kansas located near Liberal. It consists of about 2,000 acres of both irrigated and dryland farm. We also have a swine farrow finish operation.

I would like to thank this committee for having the foresight to bring a little bit of rain into the State. And also to get the information direct from the individuals that probably the drought situation has a disastrous effect on.

I would like to take a few minutes to look at the disaster as the farmers face it today. Still reeling from a near disaster in rural America, farmers and ranchers find themselves in another no-win situation. As the price of wheat approaches the level of 1980, when President Reagan took office, the producers that are involved now see a situation that many of them are not going to benefit from that price of approximately $4. I guess it would not make any difference if the price of wheat was $10 if you do not have any, and that is certainly what I am hearing from a lot of people.

As harvest time nears and corn and milo planting time is upon us, we find ourselves in a dilemma. This reminds me of something that I kind of dreamed up myself, I guess. But you know, we have the foresight and the propensity to put men in a spaceship and send them to the Moon. We had never been there before. They go to the Moon and return and then land within a few feet of where they are supposed to, yet probably in the past 35 years we have had farm bills that we have absolutely no control over. Whatever happens just happens, and that is the way it is. So I believe with a little bit of diligence and a little bit of intelligence we can certainly write a farm bill that is far better than the one we are receiving the effect of presently.

As the price of wheat approaches those levels and harvest time nears and these rains have come, we can see a little bit of light at the end of the tunnel, but as I have visited here today with a lot of people throughout the State, many of them did not receive near enough rain. In my area we got nearly 4½ inches, but I talked to somebody that lives around here that says they got less than 1 inch. With 1 inch there is certainly not too much prospect of planting spring crops.

I might give you a little bit of insight into what our farming operation consisted of. Last fall we planted 635 acres of wheat. As of this date we presently have about 450 of that left. I expect that yield to be less than 10 bushels to the acre on the remainder of that. On most of my rented land I will be required to give a third of that to the landlord. That is going to leave me with about 6 bushels to pay the expense, and it will take about half of that to run the combine across that stuff. That is our situation.

We carry no crop insurance. We never have. I never have. I guess dad did back in the early 1950's. He became dissatisfied due to certain rules and regulations and restrictions on that, and that was clear back in the 1950's and since that time we have not carried any type of crop insurance.

As I recall, I started farming full time in 1961 and probably this is the first real disaster that I have seen as far as it has put many people clear out of business and will harvest zero acres. That is one reason that we have not had the crop insurance. I know there is quite a discussion about whether it should be mandatory or not. That can be debated at a later time.

On May 9 we went into the local ASCS office to certify our acres of wheat, and at that time we made the decision to destroy 160 acres. I can say that after this rain there is a possibility we might go back and destroy some more due to the problem that was discussed earlier about the wheat and that kind of a situation.

But we had two options at that time. One of them was called 0/92 and the other one was just a disaster and plant back in milo. If we went 0/92 the payments would be some $13.50 an acre, which would—well, barely cover the cost of the fertilizer that was involved in the thing. That was the only option on that. We could not plant it back to milo. We would just have to flat out collect that $13.50 cash payment and we were through until this fall when we planted in wheat.

The logical solution to our problem seemed to be to disaster it and hope that mother nature provided the rain and that we would plant milo and hope to harvest some kind of a crop this fall. That was the decision that we made, and thanks to mother nature and somebody's good guess, I guess we probably did receive sufficient rain to plant that crop in the next few days, but on the other hand, we still lack a long way of being out of the woods because of the depletion in subsoil moisture. We are going to have to have rain, and I hope that Mike Smith's weather forecast is right and southwest Kansas does get that rain in July, because that is when we really need it.

That is part of the situation there that we have involving our family farm operation.

I have talked to many farmers across the country in my travels from where I live to Kansas City, and from Amarillo to Denver. I can see no better prospect in those areas than I can see here. I told Hap Larson on KBUF radio some time back that I thought the farmers that I talked to, we indicated the percentages of yield that they thought and it looked to me like we would produce somewhere between 120 and 150 million bushels of wheat in the State, and I still maintain as we get closer to harvest time with the rain and the weeds and other things involved, that my number is getting closer by the day.

As far as the loss to the State, there has been a lot of talk here this morning about $600 to $800 million. I have done a little calculation as far as my county, which is Seward County, KS and the possible loss of that. Our county has approximately 85,000 acres of wheat, and I would estimate that an average yield both irrigated and dryland would come somewhere in the neighborhood of 30 bushels per acre. That would calculate out to about $10 million. That is the percentage of loss according to the ASC office directory, they predicted that 90 percent of the dryland wheat was gone in Seward County and would not be harvested, and they predicted that 75 percent I believe it was, that the irrigated would not be there.

So with that calculation, and my $10 million, I estimated the loss not only in the revenue that would be lost in the wheat crop, but also the money that was put into that as far as expenses last fall in the working of the land and the fertilizing and the spraying of the bugs and all that stuff, before the cold weather hit and the winter kill and the drought situation took over. I came up within another $4 million in that, a total of $14 million.

As that $14 million travels through the economy, in Seward County I anticipate an estimated total loss of between $80 and $100 million. That is one county in the State. That is my county, and it is probably not a large county as far as wheat production. I have some information from Morris County here, and I believe they are up around 45,000 acres. They are looking at about the same situation. Our anticipated loss is something in the neighborhood of actual loss will be about $14 million.

So I believe you can see the importance of what this wheat crop can do for my county and the State and also the Nation as a whole.

I believe it should be the duty of this committee to see that the income to agriculture is maximized and not minimized. Not only in consideration of what we are talking about today but in consideration of the 1990 farm bill that we are anticipating the writing of.

I would like to talk a little bit about livestock and the situation that that involves. Many of the operations involving livestock, in the next few days they will be pulling those off of wheat, what wheat there is left, and many of them have chosen in my area to pasture off a lot of that wheat. They have to make a decision where to go with that old cow and that old calf when there is not too much decision. It is either take them off of that and take them to the sale or buy some feed, and there is not much feed available. As was indicated this hotline for the feed and forage has been established. That has been a help to some.

I would suggest the possible use of the CRP acres for haying and grazing and whatever. When you get into this, I was sitting down here listening to this, it can be a long, involved, detailed project when you get into Washington, DC, and who decides what happens. I would suggest that this committee recommend that with very few guidelines that that decision be left to the local soil conservation committee and that office director. They know better than anybody out there what can be done and what can be pastured and what cannot and I would strongly suggest that that decision be left up to those people. They know how long the grass has been there, what kind of a stand has been established, and all of that kind of thing and I think that would strongly benefit those producers used to dealing with those people.

In Seward County we have approximately 35,000 acres of that CRP grass which would not nearly all be available, but certainly a portion of it. That would be kind of a standby procedure. As I say, we got some good rain and I think in the next few weeks it will go ahead and green up and we will be able to pasture some. On the other hand, I think that will be an important tool.

I can also say there is another advantage to that possibly. As you know, the farmers are required to mow that—weeds and what have you off of there. In return for that—they receive $7 an acre I believe it is, something like that. I would think that that would certainly be a reduction. You would not have to pay that guy to do that, the $7 an acre. The livestock, would take care of that, and I can see a savings benefit there possibly on some of that.

So I would stress the importance of that because that is something we need as soon as possible due to the livestock because a cow cannot wait until tomorrow to have a drink of water or eat.

I would like to refer to a minute some of the comments from other producers that I have received. They are very few, but I think they will verify what I said to date.

I have a comment here from Daryl Miller from Edwards County which is in Lewis, KS. Daryl says that in Lewis there were 200,000 acres of wheat planted. They anticipate that 60,000 of those acres will be harvested at an estimated yield of between 10 and 15 bushels. I believe he told me their normal yield was somewhere around 30 bushels, so we are looking at 50 percent there on 60,000 acres.

In Stanton County which is way out west, about as far as you can go, Bill Wilkerson told me that 105,000 acres of wheat were planted there and the yield would be about 30 percent of normal.

In Ness County which is to the north and the west, Otto Popp out of Utica, KS; wheat in this county will yield maybe 5 to 10 bushels per acre. Cattle are a problem as pastures are not growing. This year will take out another 10 percent of the young farmers.

In Seward County, KS, Ed Strickland farms both in Seward County and also in Beaver County, OK. He said they planted 1,200 acres of wheat and had less than 200 left to harvest.

The ASCS director in Seward County, Sharon Hobble, said she and the county committee had estimated a loss of 90 percent on 43,000 acres of dryland wheat and they estimated a 75-percent loss on the remaining irrigated acres.

With that I think you can see, well I have one more here that I just received in the mail. It is not in my testimony, but if you bear with me I would read it to you. This is from Don Kress out of Council Grove. He said,

> I talked to the ASC office. They said that there had been 45,000 acres planted in Morris County and to date 15,000 had been destroyed and further abandonment is anticipated.
>
> At the Soil Conservation Office they said they expected the yield to be between 10 and 30 percent of normal with a low quality and some wheat is so short that it would not get into the combine from a sickle. Ain't it a bitch?

[Laughter.]

Mr. RICE. Some of the other things I would like to comment on was the estimates that Mr. Tunnell indicated. I had a strange phone call the other day, an elevator out of Salina, KS called me and wanted to know if I had some wheat in the bin. They had heard that I had some, which I did have. I think it gets pretty serious when the elevator starts calling you and wanting to know if you have some. They were interested in buying that wheat.

I also had a call from a gentleman out of Spearman, TX that wanted seed wheat to ship to south Texas next fall come planting time and heard that I had some. I had seen him at the—Three I—show and he was interested in that and wanted to know how many bushels I had. Those are a couple of examples as to how serious the situation is here.

With that, I believe that pretty well takes care of my comments.

[The prepared statement of Mr. Rice appears at the conclusion of the hearing.]

Mr. GLICKMAN. Dennis, I think we will hold you until last since you are going to deal with some of the credit issues. I think maybe we will wait until we get the rest of the producer groups and then we will go to you. So Pam, why don't we go ahead and have the Farm Bureau statement now.

STATEMENT OF PAMELA M. DIETZ, MEMBER AND PRODUCER, KANSAS FARM BUREAU

Ms. DIETZ. Chairman Glickman and members of the subcommittee, we certainly do appreciate this opportunity to come to you and to make a statement on behalf of our wheat and grain farmers in Kansas, and also on behalf of our livestock producers concerning those topics that you are facing daily on the subcommittee.

We also would like to thank you for your interest in the well-being of the Kansas producers and for coming here to the wheat State for this field hearing.

Mr. Chairman, I think everyone has said it, but it is dry out here. Grain and livestock concerns are immediate, and the decisions that we have to make are irrevocable.

Grain producers are facing abandoned wheat anywhere from 70 to 100 percent losses. The subsoil moisture is insufficient. Prospects of producing another crop are reduced every day that measurable precipitation is delayed. Irrigated wheat yields are expected to be down at least 40 percent because of the winter kill.

Immediate decisions are needed to be made about alternate cropping, and their primary urgency are decisions concerning the further outlay of capital for the marginal hope of harvesting fall milo and soybeans. The risks seem high and the hope seems dim.

I have included with my testimony on the back page a preparation from our local extension office about the yields of wheat, feed grain, and soybeans in Pratt County over the last 3 years. It covers acres planted, harvested, and bushels of production. Just a birdseye view, you can see that all those numbers are down, and they are down considerably.

We grain producers have been very pleased with the effectiveness of the current farm bill, and we have been especially pleased with the progressive success of the export enhancement program.

Right here in the heart of America, 1988 harvested wheat was below average in yield, and dryland milo was hit hard by the drought. We really do not want the export enhancement program to be short-changed because of the drought. We want those bushels to be there. Any drought aid that you could give us would enable our producers to till the land properly, to fertilize, and to seed at nearly normal levels.

We feel the result of this aid will be to maintain average yield and to help maintain these average reserves. Without some form of assistance, producers will be forced to seek production loans from local lenders. And in the face of these high interest rates on these loans, a lot of our ideal farming practices of optimum stewardship and excellence of product will be compromised.

The drought loss for the grain producer is of the utmost consequence. There is also the gravity of the drought on the livestock producers. You have heard testimony that cow/calf pairs are being prematurely marketed. This is causing a severe disruption of the herds that in many cases have taken decades to establish heredity and blood lines.

Water tables are lower, and natural streams have dried up. The recent showers and the mists are helping the pastures to green, but this is expected to be only temporary as the subsoil moisture still remains inadequate.

The extreme heats of July and August lie ahead. Pasture stocking rates will tend to be at one-half of the normal rate. Many are disbursing herds into neighboring States where the feed supply, pasture, and water are adequate. Our local feedlot is at maximum capacity. The owners have witnessed early January and February placements instead of the normal March and April placings. May receipts are expected to be down by at least 50 percent.

Livestock sales across the State are recognizing weekly sales of five times the number of cows normally marketed for slaughter, and this is much higher than at any other time in recent history.

Mr. Chairman, we are not only facing a critical situation here, we are experiencing an emergency. It is this crisis that causes us to respectfully request immediate action on the extension of the 1988 drought assistance package for the crops planted in the fall of 1988. Also we are asking for an extension of 30 days of the Federal crop insurance deadline for feed grain and for soybeans.

Again, we would like to thank you for the opportunity to present the views of our grain and livestock producers who are our Farm Bureau members across the State of Kansas.

[The prepared statement of Ms. Dietz appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you, Pam, for an excellent statement.

Mr. Bower.

STATEMENT OF LEROY BOWER, PRESIDENT, KANSAS NATIONAL FARMERS ORGANIZATION

Mr. BOWER. Thank you, Congressman Glickman, Congressman Roberts, and Congressman Slattery. I am the president of the Kansas National Farmers Organization. I live southeast of Pittsburg, KS. I farm about 550 acres in cultivation and another 200 acres in pasture and hay.

The drought in Kansas has reached catastrophic proportions and is probably much more severe than is being reported. The loss in the wheat crop is in excess of probably 50 percent. I will not go into details on the amount of dollar losses because it is terrific in the State. It is not only just direct losses to farmers, but it is also direct losses to the agribusiness, rural Main Street businesses, and various taxing units of the government.

I also want to commend Governor Hayden and Kansas Secretary of Agriculture Sam Brownback in their efforts to get Secretary of Agriculture Clayton Yeutter to initiate disaster legislation and other aid to agriculture.

The livestock situation in Kansas, there are excessive large cowherd liquidations going on at the present time. We also see cattle that had gone through grass and normally would have been on grass throughout the summer that had to go into the feedlots at an early date.

The recent comment by Secretary of Agriculture Yeutter that farmers should use crop insurance, let me tell you, the bottom line is that Federal crop insurance is not going to get the job done. I have had Federal crop insurance for 25 years. It is fine until you have a claim.

My experience probably, along about the first time I had to use the insurance was in September 1984. We had early frost on soybeans in southeast Kansas. This frost hit us 2 days in a row. It knocked my soybean yields from probably in the neighborhood of 30 bushels an acre down to 3.5 to 11 bushels an acre. My premium at that time was $497.77. I received $4,668. In addition to that, to make up the losses, I did have to take a loan from the Farmers Home Administration and that amounted to $17,390. In my opinion, if the Federal crop insurance had done its job then I would not have had to take the disaster loan. That is my opinion anyway.

The problem is that you are only protecting the bottom line of your production expenses. I am just trying to point out the shortcomings of Federal crop insurance.

Another thing, you can look at, the Federal crop insurance if it had been doing its job, you would have had 75 or 80 percent of the farmers enrolled in the program. If it had been beneficial they would have been enrolled in the program.

We do favor extending the 1988 Farm Drought Disaster Assistance Act to include all crops harvested for the 1989 crops. There was one point mentioned that I was told to get across here and I think maybe Congressman Roberts has the point but I will mention it again, farmers had to, had until April 14 to sign into the program. They had a choice on the 0/92 option, whether to take that or not. Those that did go ahead and choose to enroll in that program have another deadline of June 1 as I understand it, to either go or no go. If you get a disaster bill passed, of course the disaster bill if it is anything like it was in the past, you need to get that 0/92 null and void that the farmer had done, or at least make a decision on that because that did fall in a "gaposis" you had last year and there was no correction to that. I think Congress has the intent of doing things, but bureaucrats have another intent of doing it their way, too. That is one of the points I was wanting to get across.

As long as you are shaking your head and understanding, I do not think there is any need of me going through the details on it.

Mr. GLICKMAN. We understand that. We will make a point on that one. That obviously has to be a key part of any disaster program.

Mr. BOWER. That is the end of my statement on the drought. I do have a statement that I would like to read in the record if it is possible.

Mr. GLICKMAN. If you have an extra copy of the statement, we will put it in the record and we will all review that.

Mr. **Bower**. This is on new farm legislation for the 1990's and it is mainly prepared by Chuck Frazier, our Washington lobbyist. It is out of the results of the conventions that we have had.

There is one point in here I would like to make. It says switch from acres to bushels or pounds in setting farm bases. Goals in determining performances, use performance certification and spot checks to administer the program.

It was mentioned earlier that we need some flexibility in our cropping plans. To me this would offer us an ability to give this flexibility.

With that I will close.

Mr. **Glickman**. We know Chuck very well.

Mr. **Bower**. You can get copies from him for the record.

Mr. **Glickman**. Thank you.

Mr. Giessel is here. He is not only a friend representing the Kansas Farmers Union, but is a member of the National Commission to Reform Crop Insurance. [Laughter.]

We are delighted to have you here.

STATEMENT OF TOM G. GIESSEL, VICE PRESIDENT, KANSAS FARMERS UNION

Mr. **Giessel**. Thank you very much.

I am Tom Giessel, vice president of the Kansas Farmers Union. Kansas is one of 26 States with membership in the organization. And as you said, and I reluctantly admit, I am a member of the commission for the improvement of Federal crop insurance. Maybe we can touch on that a little later.

Mr. **Glickman**. I would point out that we do have another Kansas on that group, Bill Rogers. Kansas Farm Bureau.

Mr. **Giessel**. Right. I am a full-time farmer. Together with my brother and our wives we operate about 3,000 acres of farm and grassland near Larned in Pawnee County. We raise wheat, alfalfa, milo, primarily dryland but some irrigated. I believe we truly typify the true family farm in the Midwest, not only in size, but in type of operation and character.

I would like to turn to a more detailed look at how the weather has affected our farming operation because I believe what has happened to us has also happened to many other farmers in the Great Plains area.

We went into fall seeding of our winter wheat last year knowing we were short of moisture, both surface and subsoil. Our only hope was to have a good old-fashioned snow-filled winter, along with an abnormally wet spring. Unfortunately, we struck out on both accounts.

We had a very dry and mild winter which brings in its own set of problems with insects, and especially greenbugs in our area. Our spring was a siege of well above normal temperatures, punctuated by wild fluctuations, up to 100 degrees in 24 hours. Three weeks ago, following 4 days of 100 degree temperatures, we woke up May 1 to a 28 degree temperature, a hard freeze, which just about wrote the final chapter on any of the respectable wheat we had in the area. We still had little or no precipitation.

In 1988 we received about 8 inches of rain where we live, and normal for our area is about 23. In fact my home place where I live, I counted back, because I keep track, we went 309 days before we finally recorded more than one inch in a 24 hour period. This last week of rain broke my dubious record.

The bottom line is, our winter wheat crop is a total disaster, much worse than any other "expert" predicts. I guess the most recent crop and livestock survey estimates Kansas will average 22 bushels per acre.

My father always told me that "all the old prophets are dead and the young ones aren't worth a damn." He was right. Of course he is also deceased.

It is my feeling that anyone can predict or estimate a good crop. If you are predicting a 40-bushel crop and you are 4-bushels off, it is really no big deal. It does not look that bad. But if you have a 4-bushel crop and you are off 4 bushels, that is a mistake.

Farmers, I think are the only ones that can truly recognize what the situation is. As close as we could come, we compiled an 18-county report, and there is an attached copy. Bob, our extension agent along with the help of other ASCS directors and extension agents in an 18-county region surrounding Barton County compiled this, and it lists the acres seeded, the amount of abandonment, the condition of remaining wheat, and our average yield, the normal yield. We updated this as of May 17, and believe me, this is probably the most unadulterated report you will ever see.

It showed that we in an 18-county area had 2.9 million acres seeded. Already 62.66 percent have been abandoned, and the remaining condition is 34 percent of normal, which leaves about 11 bushel average.

I will get back to that a little bit later on some other details.

Winter wheat, of course, is not our only concern. Alfalfa is a major crop in our area. Our dryland fields are in very poor condition and even with the recent rainfall, I had 2 inches and twenty one-hundredths last week, and I took a spade out day before yesterday and it had soaked in 5 inches, so we still have a problem. It is not going to yield to any consequences here because it has to start the submoisture.

Our farm raises hay for feed as well as for export. During the 1980's we have averaged normally selling between 60 and 70 semiloads of hay per year. Last year much of our dryland fields yielded only about six-tenths of a ton. As a result we sold only 16 semiloads of hay, and many of that came off of irrigated ground.

As pitiful as the year we had, the more we are looking into this year, I do not think we will be selling any alfalfa, and of course there is no crop insurance on alfalfa or rangeland. In fact we are still feeding our cowherd a full winter ration because there is really no grass to turn them out on in the 500 acres of rangeland that we lease. We have missed our early grass which is our most volume and best feed value, and there is nothing we can do about that. This 18-county report was expanded to cover the rangeland conditions which obviously are already short. Growing alfalfa, which irrigated and dryland combined showed about 41 percent of normal, and of course the dryland was much worse but when you blend the two, that is what you end up with. And feed supply on hand, which is virtually nil.

Our local businesses are already suffering in a depressed rural economy and they can ill afford the direct blow of this natural disaster on farmers. Another report I have attached by Kim Barnes, manager of the Garfield Co-op, shows for example the impact on grain elevators in Pawnee County alone. A normal storage income in Pawnee County for the eight elevators will be between $600,000 and $700,000 per year. Given the current yield estimate, that is from ASCS and extension agent, they may only share $32,000 of storage income. Divide that by 8 and you have about $4,000 each for storage income compared to $100,000 plus each.

Normal wheat harvest in our county with the multiple case they gave us of 0.28, would generate approximately $24 million in income. This year's estimate is $1.1 million. I just want to know who is going to line up to get it first.

Our rural businesses and main streets do not deserve what is coming at them, just like the farmer does not. There will be more long-term incomes.

It will take years for our rangeland to recuperate from the beating we are still taking. Cowherds severely culled or even in some cases completely sold off due to lack of feed hurts producers immediately and consumers in the long term. Alfalfa fields have been brutally damaged by drought and freeze and it will take a minimum of 2 to 3 years to get back into a normal production cycle. In fact, many of these fields that are young fields are going to be pulled out of production prematurely. Seed wheat will be a premium, and soil and water conservation with no crop residue will be extremely difficult.

My concern is for the people, our most important resource. We are by no means out of this drought. Many people are having trouble dealing with the situation, taking on extra jobs, working 20 hours a day. Mental and physical health care costs will rise. Family life will no doubt suffer. This is a chapter we cannot ignore and must address in some way.

In conclusion, let me say that an extension of the relief provided last year is definitely in order. Mr. Chairman, we do support your bill, H.R. 2232.

I have heard recent reports that we are premature on our spring crops and saying that we should not consider them. I think we need to. We are like 10 to 15 inches below normal, and you couple that with the 10 inches we should receive this summer it leaves us 25 inches behind. That means 25 inches in the next 100 days. As far as I know, it only rained like that once, and it was a long time ago. It was reported by Noah. I think he was a fisherman, not a farmer.

But like last year, the answer to our problem is much larger than crop insurance, larger than a winter wheat drought bill, and larger than a program crop drought bill. The only difference in the 2 years is that in 1988 we held an election, and I am sure that a responsible Government would not allow that to drive the need to be fair to the food producer in America.

If we do nothing, history will show we failed and failed miserably. If we do nothing, we will also be responsible for a new wave of mergers, only this time it will be America's family farms. Our family farm structure of agriculture is too important, too precious, to forfeit into the hands of a few.

If there will be any good come out of the 1988–89 drought, let us hope it gives us the opportunity to rethink our food and fiber policy and give it new direction. Hopefully, it will make us aware that what we have in America's agriculture is very special. Our land and our water, our great resources and bounty, and especially our people, are great gifts. We can no longer afford to do all the wrong things for all the wrong reasons.

Disaster relief will, in my opinion, do more than just save thousands of America's farmers and rural businesses. It will be an investment which will save consumers millions of dollars over the years to come.

More importantly, it will signal a commitment and renewed respect for our most important resource, America's farmers. Thank you for your time.

[The prepared statement of Mr. Giessel appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much, Mr. Giessel.

Dennis, it is a pleasure to have you here. You may proceed.

STATEMENT OF DENNIS L. SHIRLEY, VICE CHAIRMAN OF THE BOARD, WICHITA DISTRICT FARM CREDIT COUNCIL AND FARM CREDIT BANK OF WICHITA

Mr. SHIRLEY. Thank you, Mr. Chairman, Congressman Slattery, and Congressman Roberts.

My name is Dennis Shirley. I live in Kansas and I am the vice chairman of the Farm Credit Council at Wichita, and vice chairman of the Farm Credit Bank of Wichita, which is the ninth district. It includes the States of Oklahoma, Kansas, Colorado, and New Mexico.

Many experts have reported today on the problems caused by the drought. We are grateful for the recent rains, but they have come too late for the crops in some regions. Some regions, I understand here today, did not receive sizable beneficial rains which, fortunately, at my farm I received about 3 inches of rain.

We all have a stake in seeing the farmers through this drought. It is important that farmers succeed financially not only for their own good but for the benefit of agricultural lenders, cooperatives, rural communities, and the economics of Kansas. A rippling effect reaches us all.

We in the Farm Credit System are prepared to work for the farmers affected by the continued drought. If farmers have difficulty servicing their debts we have a number of options available to work with them. Associations may consider alternatives such as deferring payments, restructuring loans on distressed farms and ranch operations. This will be handled on a case-by-case basis depending on the financial condition of the borrowers.

Borrowers who anticipate problems in making loan payments are encouraged to discuss their situations with their loan officer and associations, and the sooner the better. Early communication lessens stress on all parties involved. It helps associations respond to a situation in a timely manner.

We want to assure the borrowers that we are prepared to work with them during any difficult period; however, the real need is for external assistance. Farmers fundamentally need more income, which lenders cannot create. Another problem we face is the Office of Management and Budget has proposed legislation which would repeal the Bumpers-Pryor-Kassebaum provision of last year.

My written statement, which will be handed out later, explains this issue more in depth. The bottom line of this we feel is a provision which cost our PCS millions of dollars. In light of the drought this is no time to be imposing that cost on agriculture.

For you people out there who may not know what happened, in the 1987 Farm Credit Act there was a provision in there to fund the Farmers Assistance Corporation, Federal Assistance Corporation. Under that they assessed the ninth district PCA's to fund that, to keep it off budget at that time to the tune of $30 million from your PCA associations out there, and which took their own funds away from them. Therefore, they had to raise your interest rate to compensate for that loss of owned funds.

The drought is also complicated by other problems facing farmers. Diesel fuel, for example, has significantly increased the price along with other production inputs. I know fertilizer I've been buying this spring compared to 2 years ago is running 35 to 40 percent higher. It has come down since they realized we have a drought out there and people are not buying it.

The prime interest rate has moved up, which will increase farmers' costs as these increases are passed through to them. The prime rate is now 11.5 percent and 1 year ago it was what, 9 percent, the highest level since 1984.

Together, all these factors are placing a burden on agriculture and action is needed. In closing I would strongly commend you and other members of the Wheat and Feed Grains Subcommittee. We appreciate today's hearings and your concern for Kansas farmers and ranchers.

I have a few other statements before I am done. I would like to read this, I don't have it written. It's just some of my own thoughts.

One thing that was mentioned here today was wheat storage on the farms. My particular farm had about 70,000 bushels of reserve wheat on that farm. My loans all matured about March 1. At that time I had to make a decision on whether to gamble on higher prices or pay them off. I thought well, it's going to take one-quarter of a million dollars to pay them off. I chose to sell that wheat rather than gamble with it, which today looks like maybe it was the wrong move. Anyway, my bins are empty.

I do have a little reserve corn still on hand, but I understand it will not be extended, so we are looking to market it pretty soon.

One other comment I would like to make also is Federal crop insurance.

Mr. Glickman. This poor man on your left. [Laughter.]

Mr. Shirley. What I am going to talk about is maybe not really his fault. [Laughter.]

At this point anyway.

I have never taken Federal crop insurance except one time, so this spring with the dry conditions and my corn production is all in dryland, no-till situations where we spray the wheat stubble after harvest and kill everything. We started planting about 3 weeks ago and it got so dry and hard we just quit. It didn't seem like it made sense to go out and put $40 an acre out there every time we made a pass.

So I went to talk to my people about some Federal crop insurance. They have my farm yield set at 45 bushels an acre. The last 5 years I have averaged almost 80 in these conditions. Needless to say, by the time I have a disaster, by the time I get to my yield I have already had a disaster, and my payments started at like 36 bushels or somewhere in there, some amount. With a low yield my costs were even higher. Given that low yield, signing up for the 1989 program with that low yield, had my yield been set at what my average was, would have made $43,000 difference in my potential payment. I call that rural development. Those moneys that come to me I'm going to spend. I am going to pay my debt off that I owe the Farm Credit System, and I owe a bunch of money, too.

Last year's corn crop, for example, and we had a pretty good corn crop and I am in sympathy with those that did not have one. Given the price I sold that corn for versus had Iowa and Illinois raised a huge crop and the prices been at the low level, and I would have received a maximum payment, there was $50,000 difference in the value there. I would have had $50,000 less income for that 1988 corn crop. Now we are starting to talk some dollars, here at least in my checking account.

So I just bring those points out to you that when you get the revenues tied up from Federal crop you get a problem with your yield. My wheat yield is not as bad. It is somewhat better. My size farm with my son involved, we still have a $50,000 limit problem. We are just a family farm. We work at it every day.

I guess I would mention one thing on the new farm legislation that I think has, that worked well for me in the 1970's. That was my allotment was not what I could plant, it was the amount of acres I could not plant. Therefore, I had the option to plant milo, corn, wheat, sunflowers, whatever. That worked well for me then. I am not sure it would work well for everybody.

In closing I would say one thing that one might want to consider when it comes to drought legislation. We are going to be hurt by allotments, by the bases as well as the yields. It is figured on those bases. But I just read in the paper the other day that the B-2 bomber, stealth bomber, one copy, is going to cost five hundred and some million dollars. If this great Nation can build a bomber that costs five hundred and some million dollars, it seems to me that when we have a drought the farmers deserve a little aid.

Thank you.

[The prepared statement of Mr. Shirley appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you, Mr. Shirley.

Before I ask questions, I would like to recognize the State legislators who are in the audience. I have seen some, but I wonder if you would stand up and just give your name and where you are from. I saw Max Rumah back there, but why don't you stand up first.

Max Rumah from Dighton.

Mr. SLATTERY. Frank Beeler was here.

Mr. GLICKMAN. Anybody else?

Mr. SLATTERY. I think they left.

Mr. GLICKMAN. We appreciate it. Frank Beeler, Roy Uhrlick, and Bob Mead were here as well.

Tom, I wonder if you could give us a status report on the crop insurance commission. When you are going to recommend something and just a little bit, you might let the folks know what is happening.

Mr. GIESSEL. This commission was a result of legislation, as you know, last year, and it gave us this big wonderful amount of time of 6 months to improve this thing. It has been a challenge. There are 21 producers on it. We have already made an initial report as of April 1 which we came up with a list of 27 recommendations that, administrative changes that can be made to improve for this corp year. We submitted them to FCIC and the Department. We ran into a few problems. Most of them they think they can handle, but there are a few they think they will have a little trouble with apparently.

But our major report will come out July 1. That will be the big one and the tough one. We have an excellent group of 21: 10 producers, 10 insurance, and the head of FCIC diligently working. We sincerely want to make crop insurance work. We think it is going to be what is.

I really am reluctant to scrap it. I think it is a risk management tool that if we put it together and get it pointed in the right direction is going to be what we have.

I might also say that we are going to deal with yields—now as APH, we have recommended to get that down to 5 years as well as give you an option between that and the ASCS yield, whichever is in your best interest. The problem we have, and it is bad, is fraud and abuse. I am one for—I want a decent level of coverage and I think everybody in this room does, but obviously we have a few that screw it up for everybody. There has been some real abuse and some real fraud so we have to be extra cautious.

We are dealing with yields. I think we will have that one handled.

I am not speaking for the commission. I am speaking as Tom Giessel, vice president of Kansas Farmers Union.

The price issue, the price selection has been, for those who may not be aware, the estimated market for the year in advance is where they work those figures. There has been a suggestion that it is tied to a certain slot of the futures market through the year. Personally I have big trouble with that because the futures market has very little bearing on my cost of production. I personally, and the Farmers Union, would like to see the price tied to cost of production figures. It would be more stable, be more realistic to the producer, and I think would give stability to the program that would help a lot.

As I say, this is not the view of the commission it is mine. In fact I am a minority.

I think ultimately, and one of the reasons that participation, we have to have participation up and that is a real problem. But we had trouble through the 1980's with the way the farm program was designed, half the people's income was automatic, so people, I think were reluctant to take crop insurance. So as we pull more people in it will help. It will be more actuarily sound which I think is one of the most important issues, to have it actuarily sound.

My personal opinion is, I think, we need to have a program at the levels the farmer needs. Second, the farmer should pay what he can. Finally, I would say that if we are going to continue with the cheap-food policy, I think the Government has to come in and pick up the rest of that premium to ensure a cheap insurance policy for the farmer. It is only fair.

So I think it is the responsibility of everyone who eats, everyone who has an interest in agriculture, to be part of that. We are asking a lot of our producers and our farmers, and I think we can make this a very workable program. Like I say, we have an excellent commission and we are working our tails off to get done by July 1.

I don't have any other comments. I would be glad to try to answer questions. We are dealing with yields and pricing.

One other thing I will briefly mention is the fact that we have proposed that we have producer boards that farmers will sit on to react to changes that need to be made within the system. A lot of these things happen in Washington, it's a knee jerk. Somebody goes over to the Department and says, we need this changed, and need this changed, and pretty soon it looks like Lego's, those building blocks my kids have got, and pretty soon it just falls apart, it's just pieces.

I think with the combination of our ideas that we will present as recommendations to Congress, that we can make this a workable program.

Mr. ROBERTS. I want to thank you, Tom, for your efforts on the commission. You and Doyle take a lot of time and you have traveled many many miles and you have heard the obvious complaints. As you know, I am not much of a fan of Federal crop. I have been—on the House Ag Committee, I guess. It has been in effect for 12 years. My predecessor, Keith Sebelius, had very strong mixed emotions when we went down that trail.

There is a fellow sitting out there about 12 rows back who is a cantankerous sort, always gives me good advice, old Joe Convert out there who made the comment several weeks ago when I met with my—county wheatgrowers and we settle all the problems of the world, and Joe makes the point, he made the observation, made the prediction that after we add up all the costs of Federal crop, all the paperwork, all the studies, all the expenditures, that the disaster program on occasion when we really have a disaster would be less costly and more effective. I am not too sure that he isn't right.

Now having said that, I know that I am the heel that is dragging upstream whatever it is on the Ag Committee with Federal crop, and we are hell bent to make it work. So we will try and make every effort to make it work. I just appreciate your time and your energy on that.

Jim, you made an excellent point on the fact that the decision in regard to grazing and haying should be made locally. In existing law, during the disaster bill last time, or whenever we had haying and grazing, SCS works with ASCS and they make that local observation as to growth, as to soil conditions, and that is what they are for. So in any grazing authority we will, as you have suggested and so rightly pointed out, be making that decision locally as opposed to in Washington or for that matter even in Manhattan.

I would make one other comment that I am very worried about, and again I am going a little upstream. It has to do with Federal crop.

When I introduced my bill over 1 month ago for disaster assistance I put the requirement for Federal crop in there. Not because I wanted it in there, because I am a realist and I count votes, and I can tell you the mood in the Ag Committee, and more importantly on the floor of the House is such that if you have a disaster bill without the Federal crop requirement you are not going to have a bill. Not on the Swanson issue. This business of saying well it was stopped by the administration or stopped by such and such on the floor, we do not need that. We need action.

But I must tell you that I am getting more than a little concerned and frustrated and downright angry over the requirements that we are asking the farmers to participate in a supply—program that is for the benefit of every consumer in this country. We have Federal crop requirements. We will have a very strong environmental section to the farm bill. I worry about that matter. We have something called LISA, Low Intensive Sustainable Agriculture, and I am all for that. We need to move toward that in a reasonable way, and it deals with pesticides, and God knows we have seen all the problems with pesticides that we have today. I am not too sure that we can afford LISA during those times of difficulty. But we may require, or give you higher program benefits if you use less pesticides or penalize you if you use pesticides. There are those in the Congress that want to do that.

We are going to require the farmer, already have required him, a great deal of things in regard to conservation compliance, and of course you cannot rotate your alfalfa or you are guilty of sod busting and all of that nonsense. We require the farmer to come under certain payment limitations. Now we are going to get in the business that we are going to give you substitution, but only if you have a triple base. That is now called the Roberts-Stenholm plan, and Roberts very quickly got out of that when he tried to figure out what it was in terms of that, that is, you get a reduction in your target price on a certain number of acres and then we will give you the substitution.

I have news for the Ag Committee and I have news for the Congress. If we keep up these requirements for Federal crop and environmental stuff and conservation requirements and payment limitations and defining this and defining that and changing the doggone thing every third foggy night, if we ever get priced in a crop I will tell you what the farmer is going to tell us, what to do with that farm program.

I do not mean to make a populist speech, well maybe I do. [Laughter.]

But this is a supply management program. Every requirement we put on for some social design or some well meaning kind of program or policy tailors again at the farmer's ability to take part in this thing and I worry about it. I really do worry about it.

I want to thank the panel, and thank everybody for coming here. That will be my closing remarks, Mr. Chairman, so we can get on down the road. Thank you, for coming to the first district, and thanks especially to you Jim, for coming all the way out here from Topeka and good old good intent Kansas where you are from. We usually have to come all the way there for all of our meetings, so thank you for coming out here. And thanks especially to all of you for taking all of your time.

Mr. GLICKMAN. We have another panel.

Mr. ROBERTS. Oh, we have another panel?

Mr. GLICKMAN. Yes. This is not the end.

Mr. ROBERTS. Oh, so I will just——

Mr. GLICKMAN. Repeat your speech later?

Mr. ROBERTS. No, I am not going to repeat the speech later. I will not have any closing remarks later, and that will be a good deal too.

Mr. SLATTERY. I too, really appreciate the testimony of the panel here today. Tom and Dennis, I sure hope you can all get your minds together on this crop insurance thing. I do not know whether we are going to be smart enough to figure out what is sensible in this area or not, but I sure hope we can. I happen to believe that farmers would like to have some kind of a sensible crop insurance program that they could buy at a reasonable price that would insure them against these kinds of disasters. I do not know whether we can do that or not, but I sure hope we can. I look forward to the conclusions of the commission that you are serving on with Doyle Rahjes comes up with. Good luck to you, and I look forward to your report on that.

Mr. GLICKMAN. Thank you all. Jim.

Mr. RICE. A little bit ago, and these three gentlemen over here don't know anything about this, but what they have is a farm survey that I have put together and I passed out a bunch of them a little bit ago. It has no return address or anything on it, but it is mine and what it is is a bunch of questions concerning different farm programs, aspects, and that type of thing. I have been doing this for 3 or 4 months.

What I would like for each one of you to do if you have one of those, or if you do not have one I think I have some more over there, I would like for you to fill those out. I am going to take these up to Washington one of these days when I go see these guys and I am going to meet with them, and I am going to show them what you people actually want on this thing. It has to do with—prices, loan rates, export enhancement programs, continuation of the farm bill, and that kind of thing.

I might mention to you one thing here on continuation of the farm bill. It says do you favor the present one. The sequel to that is right down here, for at least one more year. It is running about 4 or 4.5 to 1 right now on that. I think not necessarily because it is a good bill but because these people are so cotton picking tired of changing things. They are getting used to something now. It only takes about 2½ or 3 hours in the ASC office to sign the form and they have that down on their schedule. It is not because it is a good bill by any means, but they are ready to stick with something and fine tune it so it will work better. But that is just one of them. So I would appreciate it if you would leave them here for me.

Mr. GLICKMAN. Thank you all very much for coming.

The last panel is Dr. Art Barnaby, agricultural economist, Kansas State University; and Mr. Larry Kepley, producer, Ulysses, KS.

By the way, I want to thank Barton County Community College for their hospitality here. This is a fine auditorium and a fine facility and we appreciate very much their letting us use the facility.

Thank you very much. You are the concluding panel today. Dr. Barnaby has testified before the House Agriculture Committee in Washington and provided us a lot of input. And Mr. Kepley, it is a pleasure to have you here today. So we will start with Dr. Barnaby.

STATEMENT OF ART BARNABY, AGRICULTURAL ECONOMIST, KANSAS STATE UNIVERSITY

Mr. BARNABY. Let me start off by saying I am pleased to be here to visit with you this morning. I have submitted written testimony and most of my remarks will be in there. In fact I summarized it. It's fairly lengthy because I included some research results. Sometimes I find that people do not necessarily accept what I say as fact and want supporting evidence. So if you are satisfied with my presentation, you only need to read the summary.

First of all, the other witnesses have testified for you about the size and the scope of the losses and I have nothing to dispute that so I am going to leave it there and concentrate my remarks on two Federal programs that are in place which help farmers deal with risk.

The first one being the ASCS program, and I have a graph here. What this shows is the impact of price on revenue. The vertical axis. When you have very low prices you receive a deficiency payment and back up in this area here farmers would receive roughly half of their gross revenues simply from deficiency payments and so as you increase price the revenues drop. With a zero yield,—out of the program. So the program gives you considerable income protection with low yields if prices decline. So it's sort of like reading the economics book upside down. If you have a bad crop the best thing that can happen for you is to have everybody else in the world to have a bumper crop, drive the price down, which drives up the deficiency payment, and you retain this.

Now individual situations, if you have yields that are above your program yields, you are better off with higher prices. If you have yields, as in most of Kansas this year, below your program yields then you are better off with lower prices. It is sort of an inverted way of looking at the world but that is in fact how it works.

Where we are right now, we are up around $4 with the wheat, so this really does not help farmers as far as any help with the current drought.

That leaves us Federal crop. Congress has asked extension, who I work for, to do the job of educating farmers on it, and I think you have heard that farmers are not too happy with it. If you think that is fun going out holding testimony, go out and try to hold an extension meeting on crop insurance, and I assure you, you will get an earful.

One of the things that always strikes me in any industry is when you produce something, whether it is a service or other things, we all hope we are doing a good job. So when you give some of these criticisms to crop insurance, they do not necessarily soak in. One of the things is that no one has stood back and exactly looked at what this program covers. A lot of people think it covers yield, and it really does not. The reason it does not is because of the way they handle the price election.

Right now they are receiving $3 for wheat that is worth $4 in the marketplace, and we can see what happens right here. You are looking at a situation where we are looking at a zero deficiency payment because the price is over $4. In this example I used the 75 percent coverage level and you receive the net indemnity payment but no deficiency payment. His expected gross income is a program yield and—times target price. As we move up with lower prices, the deficiency payment starts to grow, and at the low level you can actually end up with a net revenue combined with crop insurance that is over the expected amount. So with low prices you come out very well had you had insurance and been in the program.

However, in the present situation we are looking at a zero deficiency payment and with 75 percent coverage, it is only going to cover 53 percent of that yield. And if you also look at 65 percent coverage it drops it back to about 40 percent. So the bottom line is in the current market, he is not going to cover that 75 percent of his expected income that he intended to.

It can work the other way too. You can end up, because of forecasting the price a year in advance with a price that is well over the market and in this case here, I have a situation where he is getting $2.57 in the marketplace and is being paid $3 of it is a loss. In other words, as I explained this to a group of farmers, if you have a $2 market price and you are receiving $3 for crop insurance, in other words, you get $2 for every bushel that goes in the bin and you get $3 for every bushel that goes out the back of the combine, how are you going to set the combine? That pretty well states it.

You are going to get more by losing crop.

Now any time you run an insurance program and you insure a building or anything else for more than it is worth, it is likely to burn down. This has happened. It is not the current situation in Kansas, but as recently as a couple of years ago they were paying $300 a ton over the market for raisins. It happened in 1985 on wheat in Montana, so it does cut both ways. Right now we have it below the market but it also can end up above the market.

A couple of things I have outlined in the paper on ways to address this, and these are fairly involved and it explains to some extent the length of the paper that I submitted to you, but one way would be to guarantee the estimated deficiency payments on any bushel that is lost. In other words, sort of like a 0/92 payment if you will. The logic behind 0/92 is if you do not have any yield, you have nothing to sell, so you have nothing to compare to higher prices, and so therefore, and the other thing that has to happen to make this work is Federal crop and ASCS would have to use the same price forecast. In this case here I assume they did use the same price forecast. Had they done that, that would have generated $33 estimated deficiency payment which in this particular thing would have been guaranteed on bushels lost plus the crop insurance payment or bringing back the 73 percent. The difference between 73 and 75 is the premiums, and basically cover what he thought he was going to cover when he bought the contract—over here, he only covers 75 percent.

So that is one way to do it. The deficiency payments are built into the Federal budget. So it does reduce the potential savings, but it would not be spending new money.

The question I got at that point was that's great. Can you do that without taxpayer money? So I submitted another plan and this one I am not sure—bought into the concept, but the idea would be to go ahead and insure a dollar liability amount like private hail does, $100 an acre. If it does not get a crop that is below the guaranteed level, then you start paying the losses at the market value. In other words, they can be getting $4 a bushel for those losses right now rather than the $3 that was forecasted.

Now what have I added to the program? I have added a price risk to the program. The way I have proposed that to be handled through private insurance companies is they would—price risk similar to a grain elevator. They are still going to underwrite the Federal crop, the yield guarantee, but the price list portion would be handled probably through a combination deciding how much risk they want to reinsure, if you will, for the futures market. They would not need to reinsure all those bushels because they probably would not be paying losses on those bushels for one thing. So the insurance company is going to be able to pool that together where the farmer would have to do it on each bushel he has guaranteed. It would be a combination of calls. It would involve a fairly elaborate price-management scheme similar to a private grain elevator. The idea being that the company would pass that risk on in the futures market and still be able to pay the farmer what he is trying to get to.

That particular approach does not involve taxpayer money. The only thing I can tell you about this, it is a little bit different than the way we thought about insurance in the past. It takes a little time to think through new ideas, and we are not going to do that today, but I can tell you I have some private insurance companies—and they are thinking about it. So it is a different way of doing business.

The other issue that always comes up with crop insurance is distribution. Yield guarantees. This is my own normal curve. The normal distribution curve that I guess everybody has in their statistics classes. You have about an equal chance of getting a high one as you do a low one, and everything works great.

Why is this important? For one thing, suppose those yields are not normally distributed. Suppose they are skewed. Suppose you have a long downside tail and a big—down here that is very low, zero even, and very little chance of—on the other side. For example up in Congressman Slattery's district which is where—this point, we looked at corn yields. You can get a zero yield up there, obviously. But on the other hand, the guy may have 115 long-term average yield, but he is not likely to get 200 bushels up there—soil, et cetera. So if the yield is skewed, and I think it is definite that it is, Federal crop a couple of years ago went to the business of simple average. Simple average does not hurt you if you have an equal chance on both ends of the tail, but if you do not have an equal chance on both ends of this distribution tail then it is not going to be a good deal.

So in this kind of a light, that is why I think the olympic average made a lot of sense, which they dropped in the name of simplicity. But sometimes when you go to simplicity you lose reality, and what you are doing with olympic average, for one thing if a guy gets 1 year of a loss, you do not automatically lower his guarantee just because he had a 1-year loss in an olympic average environment. The other thing with olympic average and drawing so few observations from 5 to 10 years, this has all been kicked around. Right now it is 10 years, there is a proposal to go to a 5-year average. If you go to a 5 year average, if those yields are negatively skewed then you have an even bigger problem with using simple average.

One last overhead and then I will quit. I know it is lunch time. But if you look at corn yields for northeast Kansas, we are trying to get some similar work for wheat done. But these are the corn yields as measured across the bottom, from a 50-bushel average up to 135-bushel average. These are 10-year averages. Actual farm yields—the measurement—as you can see they are virtually all negative and they are all trending downward so if you look at that thing trending downward that means with higher yields you have even more skewed distribution, and the top producer is going to really want to have an olympic average if he really understands what is going on with the skewed distribution.

I would like to take credit for doing all that original work, but Iowa State University also uses national statistics and came to the same conclusion that those yields were negatively skewed and it does have a meaning as to what they ended up with as the yield guarantee. So that is one of the problems, the yield guarantee that farmers have.

With that I am going to conclude and just say that as far as the drought aid is concerned, there are only two places that is going to come from this year, either out of farmers own equity, or if they had the foresight enough to buy crop insurance, certainly those people are going to be better off than those without, and the rest will come from equity on the farms or it will come from the Federal Government. If they have no equity left, I guess it——

Thank you.

[The prepared statement of Mr. Barnaby appears at the conclusion of the hearing.]

Mr. Glickman. Thank you, Mr. Barnaby.

Mr. Kepley.

STATEMENT OF LARRY R. KEPLEY, PRODUCER, ULYSSES, KS

Mr. Kepley. I appreciate the chance to be a part of this hearing along with the fine group of agencies and farm organizations who appeared ahead of me. I feel like a clean-up hitter at this point. As a farmer and a professional farm manager I have great respect for

Sam Brownback and the leadership he is providing for Kansas agriculture. I appreciated the opportunity to hear him on the program along with the other Kansas officials earlier this morning.

I watch Mike Smith's weather forecasts in hopes of rain almost every evening before I offer my prayers for his efforts. KSU's staff such as Jim Shroyer and Art Barnaby help us farmers to understand and cope with the drought. My farms were among the first to sign up with Servi-Tech and Rollie Stukenholtz when it was offered in Grant County.

Howard Tice and Bob Paris that spoke here for KAWG this morning and Pam Dietz, a fellow Farm Bureau member, are champions of mine. By selling grain that goes to elevators that belong to Tom Tunnell's Kansas Grain and Feed Association I feel I belong to his group also.

I am a KLA member as a hog producer and beef producer. As a director of the Federal Land Bank at Garden City and having served on some Wichita Farm Credit district advisory groups through the struggling period with farm credit, I can appreciate Charles Shirley's position as a director of the Wichita Farm Credit Bank and the interest and concern that he has in the present conditions we see in the weather patterns.

My neighbor, Homer Evans who lives 1 mile from me, being the national lobbyist for the AAM, keeps me up to date on Jim Rice and AAM's strong efforts on behalf of better farming income.

As you see by my attached résumé, I am a "joiner" and the main reason I have not highlighted Don Lundquist, Paul Bauer, and Tom Giessel and their fine farm organizations is that I have not been asked to join them as of yet. This oversite will no doubt be corrected after my comment.

As a good friend of Elmer Davis who has served with me on other committees, I don't plant soybeans, but if you can find me some seed I may correct that situation and thus be eligible to join the Soybean Association.

I use these opening remarks to reflect the perception of many of my fellow farmers who were not asked or did not request to be on this panel today. I hope to convey to the congressional delegation that has been so kind to be with us today, some commonsense wisdom to the agricultural policymakers who have as much if not more control on our economic and social destiny as mother nature and the fickle weather.

In 1988, I received Federal crop insurance payments and Commodity Credit disaster payments on some of my dryland wheat; hail insurance on some irrigated wheat; and commodity credit disaster payments and Federal crop insurance on some of my irrigated corn that was hail damaged. Because of insurance availability and my management decisions I am still able to put out a crop in 1989.

My farm net income for 1988 was barely on the profit side. Insurance is not designed to make money if collected, and I fully understand that economic concept and concur with its intent. It would appear that 1989 will be the poorest I have ever experienced in wheat production and will be similar in yields to 1955, and 1936 to 1938 on our family farm. Drought and freeze have left our wheat stunted or dead. Small showers the past 3 weeks have given us minimum hope that we may get the irrigated milo to grow. We have not received enough to plant dryland milo and expect a harvestable crop.

Rain and snow effectiveness on our farm, as in much of the high plains, is a function of total amount received for the growing season, but more importantly, the individual event quantity, the amount that gets into the root zone, and the number of heat units at critical growing periods. I would say that Rollie Stukenholtz and Mike Smith did a very fine job of highlighting those factors.

My dad has kept very detailed weather records for over 50 years and his father for some 50 years earlier. In 1988 we received 14.03 inches of moisture with 5 rains of just over 1 inch. Two of those occurred in June, and three in September.

From October 1, 1988 to May 1, 1989—211 days—we had 1.35 inches of moisture with the most at any one time of 0.40 inch. The July 1, 1988 to May 1, 1989 moisture was 7.64 inches. Dryland subsoil as well as surface moisture is nil. The last week's rains certainly gave us some hope for surface moisture, particularly on the irrigated ground that we had already prewatered and had planted but were real concerned that we had enough moisture to bring that crop up.

I have faith it will rain and western Kansas and the high plains will bloom again. Our efforts today are aimed at how best to survive in the interm with help from national policy implementation.

Individual farmers for the most part are not in a very solid position economically, nor are their financial backers such as bankers, farm suppliers, or landlords, to come through the present weather crisis. They all have experienced the lingering severe economic period of the past 10 years that has left them with old machinery, tired old bodies, lower living standards than the bulk of their city customers, and for many, a very pessimistic attitude. We have no savings or income reserves to fall back on to get out the next crop. The May 14, 1989 Wall Street Journal says that 40 percent of the Farm Belt is threatened by this year's drought.

What is needed?

A. The 1985 Food Security Act was a very comprehensive effort by agricultural policymakers to address the needs and wants of consumers, Federal budget makers, politics, foreign markets, ecologists, agribusinesses, financial institutions and maybe not least the American farmers. There continues to be refinements to the original act. I believe with implementation of laws in place and some added refinement legislation, disaster and drought relief can be better provided to agriculture.

As near as I can determine the cost of production studies that are used to partially base the target prices of grain do not consider an allowance for risk of a natural disaster either as commercial crop insurance premiums or as a self-insurance risk factor. The target prices were set in 1985 based upon 1984 and earlier cost of production levels and are outdated. The target prices have been reduced since 1984 for reasons that had no economic relation to grain production costs.

According to the Southwest Kansas Farm Management Association figures gathered from dryland wheat farms, the cost of wheat production has gone from $55.15 per acre in 1986 to $72.22 per acres in 1988. The average production in 1986 was 30.8 bushels per acre, 1987 was 36.1 bushels, and 1988 was 26.5 bushels, 1989 average production will be less than 20 bushels per acre, but with little if any reduction in production costs.

I need to define that the Kansas Farm Management Association costs quoted here do not include an allowance for risk, operator labor, land return or management return which are generally, in an economic sense, considered valid inputs to production in any other business.

I believe the target prices need to be increased to reflect more realistic grain production costs.

The 1985 act as implemented encouraged farmers to carry Federal crop insurance on 65 percent of their share, and this is subsidized to the extent of 30 percent by USDA. I understand, if farmers chose to take the 75 percent level, there was no subsidy and thus premium costs were at a higher level. They are encouraged to carry this through commercial insurance carriers. For many reasons this has been a poor solution in relation to the pre-1985 commodity credit disaster programs. It has created a host of paper shuffling, checking, and rechecking. It has been a most inefficient delivery system for a well intended program.

This year eight landlords and I have Federal crop insurance. Each contract has to have a CCC AD1026, and I'll be glad to explain what that is if any of you are not acquainted; last year's crop production; an individual application; individual premium notes; and a yearend proven production report filed if there is no claim. I have had six phone calls from a landlady in Seattle, WA, trying to get all the paperwork straightened out on hers this year.

Last year when I had a claim, I had field inspections three times. I carried this with Farm Bureau. They were on the farm for the first-field inspection. I was fortunate enough to also have that claim audited by OMB so they had a field inspector. Then Farm Bureau came back for the final inspection. I had four trips to the local ASCS office and four trips to the Farm Bureau Insurance Office to settle the claim.

The pre-1985 Commodity Credit disaster program required one inspection and a production claim form to be filed. The old system was much more efficient than the Federal crop insurance/disaster program combination. I think the old system should be back in the 1990 Farm Act.

B. Continue the 1988 disaster program for crops grown or planted in 1989. While it is cumbersome and is delivered rather inefficiently, it is generally perceived as national budget affordable. I know that is a consideration for the subcommittee here and the Agriculture Committee as a whole.

C. Try to maintain grain stocks under loan in a broad base of storage facilities as possible to give storage income to local facilities and to be available for needed livestock feed in areas under drought stress. Both KLA and Tom Tunnell's organization have mentioned this to you and the importance of it.

D. Expand drought feed and grazing allowances to farmers and ranchers who qualify and need this help as soon as possible. Every day's delay means reduced gain, stunted calves, and poor fertility cows.

E. Expand FmHA disaster loan funds to help those farmers that can qualify.

F. Expand SCS and rural water district programs and funds or redirect existing funding to develop agricultural and domestic water supplies in drought areas.

G. Federally fund expansion of the western Kansas muddy roads rain enhancement and hail suppression cloud seeding projects. The people not familiar with that, it is a locally funded organization that has been in existence for I think 13 years now. It has shown a moderate amount of success as far as enhancement of rain, and even more dramatic results as to diminishing hail loss. I think this is a program that needs to be looked at on a wider and probably a multi-State basis rather than in a regional area in Kansas.

H. Ask the Federal Energy Commission to help irrigators using natural gas to pump water to be able to buy it at affordable prices. Federal Energy Commission Order 451 and 436 as implemented by the gas companies have caused natural gas to be priced so high that irrigation has been curtailed in many high plains areas. Congressman Glickman, H.R. 658 passage that you are a cosponsor on may also give some price relief to farmers. I have studied the bill and I would like to have more discussion.

I thank you for your time, and for listening to my presentation. I would be very receptive to questioning or a chance to expand on these remarks at some future date.

[The prepared statement of Mr. Kepley appears at the conclusion of the hearing.]

Mr. GLICKMAN. Thank you very much.

Before I ask any questions I would like to put a statement in the record at this point of Mr. Jim Pelton who is president of the Colorado Association of Wheat Growers, who is here. We appreciate the fact that he came over here for this hearing, and his statement will go in the record.

[The prepared statement of Mr. Pelton appears at the conclusion of the hearing.]

Mr. GLICKMAN. Just one quick question, Dr. Barnaby, have you submitted any of your thoughts to the National Commission on Crop Insurance?

Mr. BARNABY. Yes sir; I sure have. I have talked to Doyle Rahjes at length and also Tom Giessel. They probably have more information from me than they really want because I tend not to be too brief sometimes on my written remarks, so they have a lot of information.

Mr. GLICKMAN. Thank you.

Mr. Kepley, we appreciate your remarks.

Mr. Slattery.

Mr. SLATTERY. I do not think I have any questions, but Dr. Barnaby, I really appreciate the work that you are doing in this area. I intend to read this rather voluminous document.

Seriously though, I hope that you all can do something in this area.

Mr. BARNABY. One comment I might add is that we talk about farmers purchase or participation in the program. There have been a couple of things policy wise that have discouraged it and I have included them in the remarks. One was I got caught up in, initially they were going to deny insured farmers from going into 0/92. That has been recently changed, but by the time it goes through the coffeeshop three times you know where it comes out.

The other one is the emergency feed program. They count crop insurance proceeds as inventory and deduct it off of your emergency feed payment. Now I was told that ASCS was going to correct that, but I checked in the last day or two and that is still on the books and that is still the rules.

So again, if you are going to encourage people to buy crop insurance, you need to tell the USDA to stop cutting other program benefits. You almost need a law that says thou shalt not cut other government program benefits if they buy crop insurance, period. Maybe they would understand that.

Mr. GLICKMAN. Let me thank you for your testimony, both of you, very much.

Mr. Roberts do you have any supplemental closing remarks?

Mr. ROBERTS. No, I do not.

Mr. GLICKMAN. Mr. Slattery.

Mr. SLATTERY. Just very briefly. I think this has been a terrific hearing today. I have sat through a lot of congressional hearings but this has really been outstanding and I think all the panelists deserve our appreciation for coming here today and working on their testimony.

As someone who is not a member of your committee, I do not have the opportunity to hear a lot of this stuff in detail like this and I appreciate it. There were a number of really good ideas raised here today. I think we have some work to do when we get back to Washington, obviously. There were a number of good questions that were raised. The whole question about where we are with carryover stocks in our elevators not only with wheat but with feed grains. I thought it was an interesting idea about wheat streak, which I really had not thought about, and the need for us to try and encourage producers to destroy this volunteer crop out there to help prevent that next year.

And needless to say, we are all in agreement in Kansas that we need to do something in the area of substitution. I think the three of us are certainly in agreement on that point.

I think that Tom Tunnell, just in closing, sort of said it pretty well when he said that all boats in the same harbor rise and fall with the tide. I would have to observe that in this State and in this country, agriculture is our No. 1 industry. They are the tide. And whether you are urban or rural, the fact of the matter is, in this country today, we are going to rise or fall with the tide of agriculture. That is as true today as it was 15 or 20 years ago.

I think for that reason, a lot of our urban counterparts recognize that we need to be sensitive to the kind of $600 to $800 million disaster that we are looking at here in Kansas, and I am hopeful that we would be able to move forward with a constructive legislative response in the next few weeks, Chairman Glickman.

Thank you all again for coming today. I enjoyed being here. And Dan, thank you very much for putting the hearing together, and your staff. It is good to be here.

Mr. GLICKMAN. Let me just close by saying that this hearing coupled with the Amarillo hearing provides all of the record that we need to move on a disaster systems bill. And as Pat Roberts said, we will in fact do that forthwith. As I said at the beginning, the chairman of the Ag Committee, Mr. de la Garza has told me he supports that effort. In fact, he instructed me to make that comment at this hearing today. He wanted to do that. So we will in fact do that as well.

It is clear that the loss, and potential loss, to this State and to counties in this State is profound. We will do our best to try to make up as much of this loss as we can. Unfortunately, even the 1988 disaster assistance continued through 1989 does not provide probably more than about a third of what a producer would be getting if he had a full crop. So we are not even with this assistance—unfortunately, we cannot make the producer whole. Therefore, the State and individual people will still suffer very dramatically. But we can help. We can provide some assistance so that people will be able to pay their loans off and stay in business and that is what we intend to do with this as well.

One of the things we have to look at again is this whole issue of what we do long term with crop insurance and disaster assistance. That is a big challenge for us as we write the 1990 farm bill.

Mr. Kepley, you are right, there is so much confusion in the operation of the crop insurance program that one might think it would be simpler just to go back to a disaster program, but there are politics involved against going back to the straight disaster program as well.

We have our work cut out for us. As I said before, I was telling one of my colleagues from Massachusetts, I was going out for a drought hearing and he said, "Drought? I saw people being washed away in cars on the evening news last night." But I think we are going to be able to convince them that that is a phenomenon which does not affect our crop situation.

So I am confident we can move on this. These hearings have been very useful to us. I appreciate the fact that so many of you stayed the entire day to listen to us. I appreciate the excellent testimony we had from everybody. The hearing record will remain open for 1 week if anybody wants to give us any additional statements to be put in this record.

So, thank you all for coming. The hearing is adjourned.

[Whereupon, at 12:30 p.m., the subcommittee was adjourned, subject to the call of the Chair.]

[Material submitted for inclusion in the record follows:]

(14) The Board has reaffirmed through formal resolution its long-existing policy of excluding members with histories of significant trade practice abuses from participation on the Board and major Exchange disciplinary committees.

The Board has long had a policy barring members with a history of significant trade practice sanctions from participation on the Board itself or on either of the Exchange's major disciplinary committees, the Floor Governors and the Business Conduct committees. The Exchange is committed to maintaining the utmost integrity of the self-regulatory disciplinary process and those who administer it. To insure that there is no doubt concerning this continuing commitment, the Board has approved a formal resolution approved by the Exchange's Rules Committee reaffirming and formalizing this long-existing policy.

Floor Practice Enhancements

The Board of Trade has historically adopted all its Rules, especially trade practice rules, to meet the highest standards of both integrity and market efficiency. Existing rules proscribe unjust and inequitable trade practices, forbid trading ahead of customer orders, insure that any profit resulting from the erroneous execution of a customer order goes to the customer, prohibit pre-arranged and accommodation trades, as well as prohibit all other forms of trade abuse. The Exchange believes that these existing Rules are more than sufficient to deal with all potential trade practice abuses. Nevertheless, as part of the on-going review of all Exchange operations, the Board has approved several enhancements to floor practice regulation.

(15) All broker associations must be registered with the Exchange.

Associations of floor brokers sharing profits, expenses and losses -- particularly with the inclusion of local traders -- do not exist at the Board of Trade to the best of the Exchange's knowledge. Such associations do exist at other Exchanges and present those Exchanges with unique self-regulatory challenges to insure market integrity. The potential for abuse of customer orders and market efficiency due to broker groups is, therefore, not present at the Board of Trade.

However, some independent brokers at the Exchange do share order decks to facilitate customer order execution especially in options contracts where liquidity in deep out-of-the-money options is thin. Others share the expense of common clerks. To insure that these arrangements do not evolve into potentially abusive ones, the Board has approved that all associations of brokers which share income must register with the Exchange providing certain information to enhance surveillance of their activities.

The Board is committed to preventing any potential abuse of customer orders which would result from the otherwise legitimate business relationships of member floor brokers.

(16) The Exchange has approved a modified closing call rule to enhance the efficiency of the market close.

Market-on-close orders, if entered late, can create problems in achieving an efficient, narrow and accurate closing range. Efficient closing ranges are essential to the commercial usage of futures contracts, especially as a pricing mechanism for cash market transactions. The addition of the modified closing call provides an opportunity for such late entered orders to be completed and for individual floor traders to "even-up" after providing liquidity for closing orders. Also, a more efficient closing range facilitates a more accurate settlement price which frequently is the basis for cash market pricing.

New Regulation 1007.02 would establish an additional two-minute trading period for all contracts at the conclusion of trading sessions. During this period, transactions could take place only at prices within the previously established closing range. No new orders could enter the pit, but cancellations would be permitted. Stop orders and limit orders elected by the closing range could be filled during this period.

The Exchange believes that the establishment of a modified closing call will benefit public customers for a number of reasons. First, more efficient closing ranges benefit cash market pricing. Additionally, because the new procedure will enable individual floor traders more readily to adjust their positions (to "even-up"), they will be more willing to provide liquidity to the closing public orders at the most competitive prices. Finally, no trade made during the modified closing call would be advantaged over those made previously in the market due to the restriction of prices to those established previously by the closing range.

The Exchange also notes that the audit trail for the modified closing call will be precise because the closing call period will receive a separate CTR designation, thereby enhancing the Exchange's surveillance capabilities for this period.

(17) The Board has approved prohibiting floor clerks from having trading accounts.

Floor clerks are responsible for the clerical handling of customer orders and other trade documents. While having no trading privileges, clerks are nevertheless intimately involved in the trading process. Because of that involvement, clerks are often tempted to trade for their own account. While such trading has historically served as a valuable means of apprenticeship training to become a member, the Board has determined that the rights of membership trading must be restricted to those who pass the intensive membership admission process. Therefore, the Board has approved prohibiting floor clerks from maintaining trading accounts.

Additional Technological Enhancements

The Board of Trade has not limited technological innovation to the creation of CTR and CTR-Plus. The Board of Trade is one of the most technologically advanced marketplaces in the world. Two aspects of that technological supremacy are worth noting in the present context.

(18) The Exchange's electronic order-entry system ("EOS") will not only increase the efficiency of customer order execution and clearing, but also the accuracy of CTR.

For many months, long before the current news of a grand jury investigation, the Board of Trade has been developing an advanced, electronic order-entry system ("EOS"). Electronic order-entry will speed communication of customer orders to the trading floor, expedite confirmation of execution back to the customer, and submit trades for clearing directly. These enhanced efficiencies will not only serve customers better and reduce FCM expenses, they will also provide a computerized record of customer orders with times accurate to the second. This enhanced timing will improve the accuracy of the CTR audit trail and, therefore, the efficiency of the CTR-Plus surveillance system.

Approved by the Exchange membership on November 10, 1988, EOS is now on a prototype basis. As use of the system grows, accuracy of CTR data will be enhanced even further.

(19) The Board has approved further, intensive investigation and development of a hand-held trading terminal.

Just as EOS will enhance customer order time data, a hand-held computer terminal to replace trading cards would not only provide on-line clearing of trades, but also unimpeachable trade execution timing to the nearest second. However, no current technology exists to create such a device for use in the auction market. For this reason, the Board has approved significant expenditures of Exchange staff and member committee time to work with outside professionals in developing such a terminal to meet the needs of our markets. Preliminary work has already begun. Hopefully, these efforts will lead to the development of suitable technology within a few short years.

H.R. 2869

On July 12, 1989, Chairman English and Representatives Coleman and Penny introduced the "Commodity Futures Improvements Act of 1989," H.R. 2869 (attached hereto at Appendix 4). The bill proposes to amend the Commodity Exchange Act (*inter alia*) to improve the regulation of futures and options trading, restrict potential customer abuses, reinforce development of exchange audit trails and establish higher standards for service on governing boards and disciplinary committees of self-regulatory organizations.

During a June 29, 1989 press conference preceding the introduction of the bill, Chairman English noted that this Subcommittee's inquiry "found that the system as a whole is sound" and that "the real goal is to produce strong incentives to the industry so that we can protect against these kind of wrongs." Representative Coleman stated that the focus of this proposed bill is the "restoration of integrity which has been questioned by the media and customers."

The Chicago Board of Trade concurs wholeheartedly in the objectives of the bill and the approach of providing incentives to the industry to protect against potential market abuses. However, several provisions of the bill present seriously damaging approaches to achieving our common objectives. If enacted, these proposals could prevent U.S. futures markets from serving their public interests and meeting successfully the challenge of foreign competition. Therefore, we urge the Subcommittee to re-examine and revise several proposals, especially those relating to dual trading and audit trails.

Dual Trading

H.R. 2869 proposes (in pertinent part) amending Section 4j(1) of the CEA (7 U.S.C. 6j) to prohibit dual trading by a floor broker in any contract market trading in excess of 7,000 contracts per day based on a six month moving average. The CFTC may increase or decrease that threshold level based upon a determination that the prohibition upon dual trading creates undesirable price volatility, unacceptable widening of bid-ask spreads or otherwise threatens the public interest.

Under Section (D), the bill proposes to permit the Commission to exempt a board of trade from the dual trading prohibition if the exchange can demonstrate to the Commission that the Exchange's audit trail can detect "*any and all* instances of trading violations which the Commission determines to be attributable to dual trading and is *fully* verifiable." (Emphasis added.)

Section (C) of the bill requires the Commission to periodically determine whether dual trading should be permitted and, if so, under what terms and conditions, for those contract markets trading below the 7,000 contract per day level. Section (B) of the bill sets forth the determinations the Commission must make in those contract markets where dual trading is prohibited. Subsection (vii) provides a floor broker may dual trade if a customer designates an individual floor broker by name in writing on at least an annual basis.

Initially, any proposal to ban dual trading should be studied carefully subject to extensive expert input. As discussed previously, dual trading provides a valuable market function which should not be summarily abrogated without extensive input and evaluation. At a minimum, this Subcommittee should review, consider and have hearings regarding the Commission's study of dual trading as well as those of other experts in the field.

Assuming the Subcommittee deems it necessary to proceed without the benefit of such background, any restriction of dual trading should be predicated principally upon the ability of the Exchange to detect potential abuses. The audit trail exemption contemplated by subsection (D) of H.R. 2869 provides the framework for such an approach. However, the specific provisions contained in the bill provide an unrealistic and unworkable standard for conditioning dual trading.

By requiring the audit trail to detect "any and all" potential dual trading abuses and be "fully" verifiable, the bill establishes a standard of perfection unobtainable in the real world. Instead, the bill should be modified to reflect the objective of excellence shared as a goal by Congress, the Commission and the entire industry. The current industry audit trail is the best in the world. The Subcommittee should not lose sight of the system's existing excellence by insisting on unattainable perfection.

Improvements and enhancements are possible. Included herein is a detailed description of an extensive program of such audit trail enhancements already implemented by the Exchange. These enhancements will achieve the bill's objective of improved audit trails (an objective shared by the Board of Trade) without presenting the potential for the destruction of contract market liquidity.

The bill's audit trail exemption should be revised to be more realistic without sacrificing the common objective of maximum detection of potential trade abuses. Such revisions should include the following:

(1) prohibit dual trading unless an exchange can demonstrate that its audit trail is verifiable to the nearest minute to at least the 90% level as determined during the CFTC's periodic rule enforcement reviews;

(2) those brokers whose customers have expressly required in writing that their brokers shall not dual trade will be prohibited from dual trading; and

(3) should an exchange fail to achieve the audit trail performance standard, dual trading will be prohibited in those contract months which do not attain the standard until compliance can be demonstrated, unless the contract month displays low liquidity. The prohibition will not apply to those brokers who are predominantly spread brokers. For purposes of this prohibition, a member is classified as a broker or a trader on a daily basis and, intra-day, is not classified a broker until he makes his first customer trade of the day. This prohibition applies by separate contract month, for futures and options contracts separately. Members handling customer orders functioning in a clerical capacity shall be deemed to be brokers for purposes of this rule.

If these revisions are adopted, the common objective of audit trail enhancement and detection of potential dual trading abuses can and will be met. Critically, this common objective will be met without risking the destruction of market liquidity and the loss of American markets to foreign competitors.

Audit Trails

Section 201 of the bill proposes (in pertinent part) to amend Section 4g(2) of the CEA (7 U.S.C. 6g) by requiring that the trade time execution required by the section be verifiable and stated within a one minute increment within one year of enactment and a thirty (30) second increment within three (3) years of enactment. Paragraph (b) of the bill amends Section 5 of CEA (7 U.S.C. 7) to condition contract market status upon this requirement.

As stated earlier, the Board of Trade shares the Subcommittee's desire to have the best audit trail obtainable which does not negatively impact the functioning of the market. Requiring standards unobtainable by present technology only sets up the market place for failure, to the detriment of all involved. Deferring the requirement provides no solution because there is no assurance that technology will develop sufficiently in the interim to meet the standard.

The Subcommittee's objectives would be better served by simply requiring that the audit trail be sufficient to properly monitor the market and detect potential trading abuses. The self-regulatory exchanges and the Commission are in the best position to determine the particular specifications of that requirement. As Chairman English has stated, "precise audit trails and responsive time reconstruction for trading are absolute necessities ...." Precision and responsiveness, then, should be the standard, not an unobtainable fixed requirement.

SRO Disciplinary Committees

The bill proposes in Section 209 to amend Section 8c of the CEA (7 U.S.C. 12c) to require that exchange disciplinary committees be comprised so that for any given hearing, majority of the hearing panel shall be of a different trading status than the respondent. Trading status is divided between floor broker or floor trader, non-floor members and staff (if any).

The effect of the proposal will be to render exchange disciplinary proceedings unfair and ineffective. A fundamental premise of British-American jurisprudence is the requirement of trial by one's peers. The Committee's proposal legislates precisely the opposite: trial by those guaranteed to be unfamiliar and inexperienced with the standards applicable to the respondent's conduct and the conditions under which the respondent's actions were taken. For example, if the respondent is a broker in the corn futures pit, he will be judged by a panel whose majority is not now (and likely never has been) engaged in floor trading of corn futures, far less brokering in that contract. Not only is floor trading itself (and brokering in particular) a unique and complex activity, customs and practices may well vary even among different contracts.

Surely the best judges of one's conduct are one's peers. Given that, it is contrary to reason and the best interests of the marketplace to require a disciplinary panel to be comprised of a majority of non-peers.

Presumably these provisions of the bill are aimed at removing the perception of some unarticulated bias in the current structure of exchange disciplinary panels. The Board of Trade is unaware of any problem of this nature, whether real or perceived. However, if the Subcommittee is convinced (for reasons not evident) that changes must be made to the structure of exchange disciplinary panels, the provisions for Board of Trade arbitration panels provide a better model than that proposed in the bill. (See e.g., Board of Trade Regulation 610.01). Those rules provide that five members of the committee be chosen for each exchange arbitration panel from four major categories: (1) floor traders; (2) floor brokers; (3) brokerage firms; and (4) commercial firms. Such a model presents significant problems in the disciplinary context which are not applicable to the arbitration process.

Nevertheless, it is a better means of insuring the necessary degree of relevant industry expertise on a disciplinary panel than the provision of the bill.

The section also provides that Exchanges deny membership on the Board of Directors or any disciplinary committee to those guilty of a "major violation of any rule" within a period of time to be determined by the Commission and requires the classification of Exchange rules as "major" or "minor" for this purpose.

The Exchange has no objection to this provision; as set forth above, the Board of Trade already has formalized its long-standing policy prohibiting members with significant histories of trade practice abuses from membership on the Board or on Exchange disciplinary committees. However, the Exchange notes that the arbitrary classification of rule violations as "major" and "minor" may distort the gravity of any given offense without due consideration to the facts of each individual case.

Broker Associations

Section 102 of the bill proposes to amend Section 4j of the CEA (7 U.S.C. 6j) to restrict trading among broker associations as that term may be defined by Commission regulation.

As detailed above, broker associations as they exist at other exchanges are not common at the Board of Trade and present no present trade practice problems. The Exchange, however, does share the Subcommittee's concern that associations of brokers that are established for legitimate business purposes not be permitted to evolve into abusive entities. Therefore, the Exchange makes no comment on this provision of the bill at this time.

Public Representation on Governing Boards

The bill proposes to amend Section 5a of the CEA (7 U.S.C. 7a) to require that "outside members" as defined by the Commission comprise at least twenty percent (20%) of the governing board of each contract market.

Given the diverse representation of the Exchange's Board of Director's as detailed above and the rules, regulations and policies insuring that diversity, the Exchange makes no comment at this time on this provision of the bill.

Registration of Floor Traders

Section 205 of the bill proposes to amend Section 2(a)(1)(A) of the CEA (7 U.S.C. 2) essentially to extend the requirements of floor broker registration to all floor traders.

In view of the Exchange's rigorous member admission process as described above, the Exchange makes no comment at this time on this provision of the bill.

Other Provisions of H.R. 2869

The Exchange makes no comment at this time regarding any of the other proposed provisions of the bill.

CONCLUSION

The combination of sophisticated computerized surveillance systems and the vested self-interest of the Exchange's rigorously screened membership in the preservation of market integrity combine to create an extremely effective mechanism for the detection of potential exchange trading floor abuses. The Board of Trade has never condoned -- and does not condone today -- any trade practice abuse. Proven offenders have always been appropriately sanctioned (including fines, suspensions and expulsions).

Nevertheless, the Board of Trade recognizes that success is an evolutionary process, not a static one. Thus, despite creating CTR and CTR-PLUS -- the world's finest audit trail and surveillance systems -- the Exchange has considered all means to preserve and improve market integrity. The result of the most recent, intensive internal study is the twenty one (21) point program of enhancements detailed herein. These improvements (and others still under consideration) will insure that the Board of Trade's markets remain the world's most efficient, liquid and economical with the highest degree of integrity and professional participation.

In considering these issues, we urge this Subcommittee to remain mindful of the potential (indeed, likely) consequences of precipitous, hastily considered action. While currently the world leader in futures markets, the U.S. could easily lose this unique and valuable industry to eager foreign competitors, if ill-considered regulation is mandated. Therefore, critically valuable trade practices such as broker trading must be carefully evaluated, especially where their value is indisputably documented and no evidence exists regarding any abuses.

In fashioning any legislation, this Committee should also look with pride to the precedent set in 1986 regarding the audit trail issue. Then, the CFTC goal of one-minute time identification was left to each separate exchange, with its differing membership and markets, to best determine how to meet that goal. The result of this management by-objective approach was the creation of CTR, the world's finest audit trail. If Congress acts similarly now after careful study, the result should be the continued improvement of what are already the world's most honest, liquid and efficient futures markets. This is the goal we all share.

Several of the provisions of H.R. 2869, especially those relating to dual trading and audit trails, appear ill conceived to achieve the stated objectives of the bill, objectives shared by the Board of Trade. Instead of the prohibition of dual trading in our most important markets, the Subcommittee should condition dual trading upon the ability of the contract market to maintain a precise, excellent audit trail, not an unobtainable and nonexistant perfect system. If such an approach is adopted, everyone's common objective of market integrity and liquidity can and will be achieved.

APPENDIX 1

Table 1

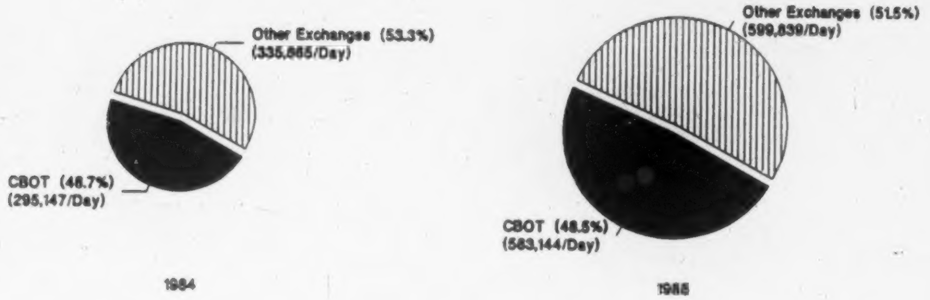
Volume Growth Rates: U.S. and World Futures Exchanges; 1984-1938

	Average Daily Volume		Growth
	1984	1988	Rates (%)
CBOT	295,147	563,144	90.8
Other U.S. Futures Exchanges	335,865	599,839	78.6
Foreign Futures Exchanges	152,000	495,549	226.0
U.S. Market Share	80.6%	71.7%	
Foreign Market Share	19.4%	28.3%	

Figure 1

CBOT Market Shares of U.S. and World Futures and Futures Options Volume; 1984 vs. 1988

U.S.



WORLD

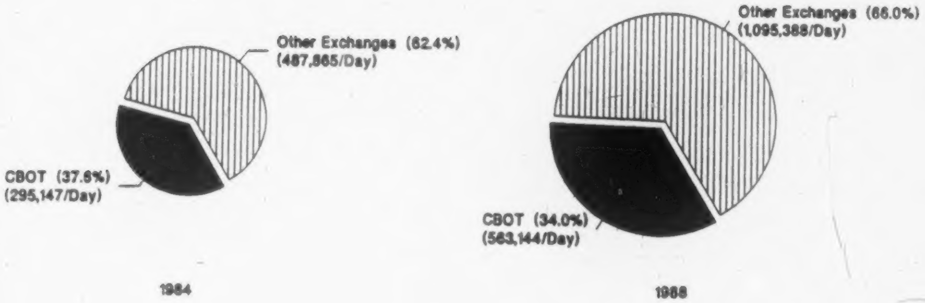


Table 2

Contracts Trading at the World's Futures Exchanges

U.S. Futures Exchanges	1984	1985	1986	1987	1989
No. of Contracts Listed	94	108	120	124	127
Growth Rate (%)		14.9	11.1	3.3	2.4
Foreign Futures Exchanges					
No. of Contracts Listed	125	129	172	178	230
Growth Rate (%)		3.2	127.7	3.5	29.2

Table 3

Ten Most Actively Traded Contracts on Futures Exchanges Worldwide 1985-1989*

Rank	1989*	1988	1987	1986	1985
1	Chicago Board of Trade TREASURY BOND FUTURES	Chicago Board of Trade TREASURY BOND FUTURES	Chicago Board of Trade TREASURY BOND FUTURES	Chicago Board of Trade TREASURY BOND FUTURES	Chicago Board of Trade TREASURY BOND FUTURES
2	Chicago Mercantile Exchange Eurodollars	Chicago Mercantile Exchange Eurodollars	Chicago Board of Trade TREASURY BOND OPTIONS	Chicago Board of Trade TREASURY BOND OPTIONS	Chicago Mercantile Exchange S&P 500 Futures
3	NY Mercantile Exchange Crude Oil Futures	Chicago Board of Trade TREASURY BOND OPTIONS	Chicago Mercantile Exchange Eurodollar Futures	Chicago Mercantile Exchange S&P 500 Futures	Chicago Board of Trade TREASURY BOND OPTIONS
4	Chicago Board of Trade TREASURY BOND OPTIONS	NY Mercantile Exchange Crude Oil Futures	Chicago Mercantile Exchange S&P 500 Futures	Chicago Mercantile Exchange Eurodollar Futures	Chicago Mercantile Exchange Eurodollar Futures
5	Tokyo Stock Exchange Japanese Government Bonds	Tokyo Stock Exchange Japanese Government Bonds	Tokyo Stock Exchange Japanese Government Bonds	Tokyo Stock Exchange Japanese Government Bonds	NY Commodity Exchange Gold 100 oz.
6	MATIF French Government Bonds	Chicago Board of Trade SOYBEAN FUTURES	NY Mercantile Exchange Crude Oil Futures	NY Commodity Exchange Gold 100 oz.	Chicago Board of Trade SOYBEAN FUTURES
7	Chicago Board of Trade SOYBEAN FUTURES	MATIF French Government Bonds	MATIF French Government Bonds	NY Mercantile Exchange Crude Oil Futures	Chicago Mercantile Exchange Deutschemark Futures
8	Chicago Mercantile Exchange S&P 500 Futures	Chicago Mercantile Exchange S&P 500 Futures	NY Commodity Exchange Gold 100 oz.	Chicago Mercantile Exchange Deutschemark Futures	Chicago Board of Trade CORN FUTURES
9	NY Commodity Exchange Gold 100 oz.	Chicago Board of Trade CORN FUTURES	Chicago Board of Trade SOYBEAN FUTURES	Chicago Board of Trade CORN FUTURES	NY Commodity Exchange Silver 5000 oz.
10	Chicago Board of Trade CORN FUTURES	NY Commodity Exchange Gold 100 oz.	Chicago Board of Trade CORN FUTURES	Chicago Board of Trade SOYBEAN FUTURES	Chicago Mercantile Exchange Swiss Franc Futures

*January - March, 1989.

Table 4

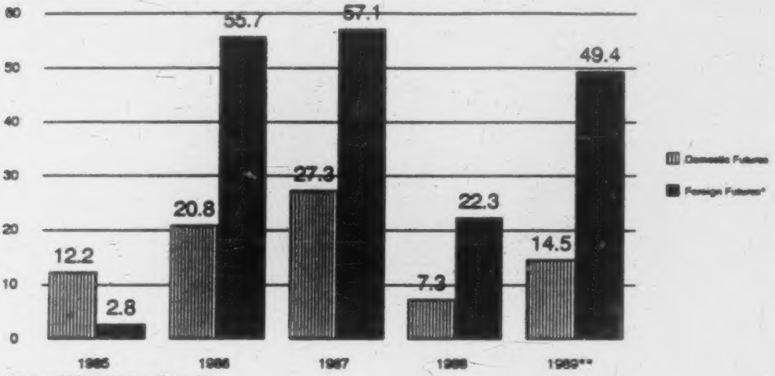
Number of Foreign Futures and Options Contracts Traded in the Top 25 by Volume in the World; 1984-1989*

1984	1985	1986	1987	1988	1989*
0	0	1	3	4	6

*January-March, 1989

Figure 2

Annual Growth Rates; 1985-1989**
U.S. Futures Industry vs. Principal Foreign Futures Exchanges*
(percent)



* TSE, LIFFE, MATIF, SFE, SIMEX

** January - March

Table 5

Volume Growth of Financial Futures and Options Contracts Trading on Foreign Futures Exchanges 1985 - 1989*

	1985	1986	1987	1988	1989*
Government Bond Futures and Options					
Average Daily Volume	13,686	77,980	171,723	189,751	218,038
Growth Rate (%)	--	469.8	120.2	10.5	14.9
Stock Index Futures and Options					
Average Daily Volume	1,590	6,655	59,914	47,428	75,305
Growth Rate (%)	--	318.6	800.3	-20.8	58.8

*January-March, 1989

Table 6

FOREIGN COMPETITION

Treasury Bond Futures Volume; Chicago Board of Trade
and London International Financial Futures Exchange
October 1, 1987 to October 30, 1987

	Chicago Board of Trade			LIFFE
Date	Night Session	Day Session	Total	Total
10/01/87	23,466	261,753	285,219	5,970
10/02/87	9,047	368,448	377,495	995
10/05/87	10,963	267,009	277,972	4,336
10/06/87	7,623	244,259	251,882	7,890
10/07/87	10,522	362,278	372,800	8,525
10/08/87	10,626	442,189	452,815	6,891
10/09/87	15,363	308,742	324,105	7,775
10/12/87*	10,370	84,586	94,956	3,391
10/13/87	14,887	278,275	293,162	6,317
10/14/87	12,100	511,021	523,121	14,482
10/15/87	19,270	640,217	659,487	12,538
10/16/87	21,967	365,532	387,499	2,461
10/19/87	28,892	483,949	512,841	13,503
10/20/87**	28,269	34,487	62,756	47,082
10/21/87	44,552	311,180	355,732	15,955
10/22/87	13,933	366,911	380,844	12,465
10/23/87	28,266	323,253	351,519	16,079
10/26/87	19,203	272,409	291,612	12,529
10/27/87	20,937	280,655	301,592	13,398
10/28/87	15,270	337,029	352,299	10,900
10/29/87	15,542	224,911	240,453	9,537
10/30/87	17,400	220,040	237,440	7,352
Average Daily (Year-To-Date)	12,385	286,505	297,121	6,186

* Columbus Day; Banks and some financial institutions closed.
** Day session locked limit up.

(Additional attachments are held in the committee files.)

150 GRAIN EXCHANGE BUILDING MINNEAPOLIS, MINNESOTA 55415
TELEPHONE (612) 338-6212

Minneapolis
Grain Exchange

TESTIMONY

of

JAMES H. LINDAU
President
Minneapolis Grain Exchange

Mr. Chairman and Members of the Subcommittee,

I am James H. Lindau, President of the Minneapolis Grain Exchange. This Exchange was established in 1881. It is an active cash grain trading center, and maintains futures contracts and options on Hard Red Spring Wheat and futures contracts only in White Wheat, Oats, and High Fructose Corn Syrup.

I note that representatives from six other exchanges have already testified before this Committee in connection with this year's CFTC reauthorization. I will limit my remarks to issues of major concern to the Minneapolis Grain Exchange.

First, a general comment. I am the newcomer in representing an exchange in a setting such as this but I am familiar with business and government. The futures industry today -- with all its size, strength and variety -- owes much of its growth and credibility to the action of this Committee in 1974. In that year you crafted legislation to create an exclusive, independent regulator to regulate the nation's future markets. The child of that legislation, the Commodity Futures Trading Commission, has done a good job under difficult circumstances. However, we are concerned that parts of this bill serve to revise the 1974 mandate and put micro-management of some aspects of the industry in the Congress and out of the hands of the expert regulator. This appears to me to be bad business and bad government.

Specifically, dual trading is essential to preserving liquidity in our futures contracts. Dual traders are involved in every aspect of futures trading at the Minneapolis Grain Exchange. They cannot be separated from trading in the current option, or spreading against deferred options, and permit retention of any semblance of liquidity. If dishonesty springs from dual trading, we must increase our vigilance to prevent it (even though there is no evidence of dishonest dual trading at the Minneapolis Grain Exchange.) If dishonest dual trading springs from highly liquid, active futures markets, let us identify and punish the dishonest traders, but let us not, in the process, destroy the futures markets. These markets have provided the best, and often the only, source of pricing information and margin protection dating back almost to the Civil War.

Technology is reaching the point that very accurate, timely audit information is available to help identify those traders who might try, unfairly, to do better than their trading skill alone might permit. At the Minneapolis Grain Exchange, we believe that our audit program provides a satisfactory means by which to verify the timing data submitted to the Clearinghouse and to detect inaccurate or missing trade data on source documents.

In this regard, the Commission, during its 1988 Rule Enforcement Review of the Minneapolis Grain Exchange, found that the Exchange's one minute timing system was extremely accurate. The CFTC stated, "... the Exchange's overall average accuracy rate was 96.8 percent." We believe that an accuracy rate of 90% or greater is a proper target, and will, of course, continue to strive to maintain a high level of performance in this area.

Let me take a minute to congratulate Mr. Cherry and his staff on their professionalism. We were visited at the Minneapolis Grain Exchange by Mr. McDonald who was competent and thorough. It is our view that the fruits of this long, detailed investigation should be fully used by the Committee as part of its responsibilities to oversee the CFTC. In the main, the CFTC has more than enough statutory authority in the areas of so called "dual trading", audit trail and composition of boards at exchanges. I think it is entirely appropriate for this Committee to review the record of the CFTC on these issues; it would be very risky to incorporate your concern in statutory mandates.

Testimony of

Sanford J. Grossman

Executive Summary

Dual trading is said to occur when an entity sometimes trades as a broker for customers, and at other times trades for its own account. Dual trading is quite pervasive throughout the United States securities and futures markets as well as in financial and commodity markets throughout the world. The pervasiveness of dual trading is due to the fact that many of the skills and facilities required to be a good broker are also necessary to be a good trader. Dual trading increases the supply of both brokers and floor traders because a dual trader can earn income from two activities to cover the costs of training, an Exchange seat, and time spent on the floor. He has less idle time and facilities when he can switch from the activity in low demand to the activity in high demand.

Dual trading has both a direct and an indirect effect on the quality of customer services. The direct effect is an increase in the quality and quantity of brokers. The fact that dual trading increases the supply of brokers means the customer has more brokers to choose from and at a lower price. Furthermore, using a broker who is a good trader means higher quality executions for customers.

The indirect effect derives from the increase in the liquidity of the market caused by the increase in the number of market makers. Parties who trade for their own account by buying at a low price and selling at a high price serve a market making function. Thus the ability for an entity to use its facilities for proprietary trading results in an increased presence of market makers on the floor at times when their services are most needed. More traders standing ready to trade make for a more liquid market with smoother price changes.

In order to aid in a comparative analysis of dual trading I distinguish two types of dual trading. The first type, called simultaneous dual trading occurs when a firm trades as a principal for its own account, and an agent for its customer in the same transaction. This type of dual trading is prevalent in securities markets, currency and interest rate swap markets, and the fixed income market. Simultaneous dual trading does not take place in futures markets. The second type of dual trading called consecutive dual trading occurs when a firm trades for customers as an agent and at other times trades for its own account as a principal, but the firm does not do both in the same transaction. Consecutive dual trading occurs in futures markets, as well as in all of the markets in which there is simultaneous dual trading.

Dual trading plays a particularly important role in futures markets as contrasted with securities markets. The fact that all trading in futures takes place on the exchange floor and that spread trading is an important part of hedging strategies make the skills of a trader more necessary for a good futures broker. The immediacy required by the futures market makes liquidity more important, and therefore makes a larger supply of market makers more critical.

There are three types of brokerage services the customer needs. The first service ("search") involves searching for the parties who are interested in being on the other side of the trade (i.e., the contra-party). The second service ("timing") involves obtaining and processing information to determine how long to wait for the arrival of the most advantageous contra-party while being exposed to the risk of an adverse price move. The third service ("bargaining") involves actively bargaining among available contra-parties to obtain the best price.

A securities broker can use his skills and sales force to prearrange trades "upstairs". Upstairs search is often an effective substitute for the downstairs working of an order where "timing" and "bargaining" skills are needed. A futures broker cannot prearrange trades upstairs. The brokerage firm cannot substitute "search" skills for trading skills. The order must be worked on the Exchange floor. The floor broker must have the ability to trade in such a way on the floor of the Exchange that he brings the other side of the trade to the floor at a good price for his customer. Therefore floor trading skills are relatively more important in the futures market than in the securities market.

Further, much futures trading involves "spreads" where a customer wants to buy and sell two (or more) contracts simultaneously for a guaranteed net price. The customer's broker can execute the spread by trading with a "local" on the floor, or the broker can execute the individual "legs" of the spread consecutively. The latter will be in the best interest of his customer if the broker is a skilled trader, since, by trading each leg himself, the broker avoids paying the local a premium for the risk in trading the spread. Such spread trading is inherently risky to a broker, since after he executes one leg of the spread his customer can hold him to a price for the other leg of the spread, which the broker may find impossible to achieve if the price moves after he does the first leg. This aspect of futures trades as well as the relatively higher underlying price volatility in many futures contracts increase the trading skills burden on a futures floor broker relative to that of a securities floor broker.

Futures trading customers often have a high demand for immediacy because they are trading to hedge an underlying spot market position. The fact that immediacy of trade execution is extremely important to futures customers implies that they will have a greater demand for market makers than will be the case in markets where the cost of delayed execution is smaller. A commodity hedger bears great risk if he does not do his futures trade immediately. This risk may force him to trade using a "market" order, for example to sell immediately to the highest bidder currently available. If there are few market makers then he will receive a relatively low price, i.e., his trade will have a high market impact cost. Thus futures markets have a great demand for traders who in effect serve a market making function. The institution of dual trading permits this demand to be met at low cost.

Dual trading increases the supply of the types of customer services which are relatively most demanded by futures customers. Dual trading is prevalent in the securities market, both on the floor and off the trading floor. Institutional securities trades are often prearranged off of the floor, and this lessens the burden of securities floor brokers. It would be quite peculiar to eliminate dual trading for futures and maintain it for securities where the dual trading by floor brokers is less important. The elimination of dual trading from futures markets will harm customers by reducing the quality of brokers who do customer business. The best traders will trade for their own account, leaving customers with brokers who are less skilled traders. By preventing traders from acting as brokers, the elimination of dual trading will reduce the number of floor traders, and thus reduce market liquidity. Foreign markets will gain an advantage over US markets causing large customers to leave US markets which will lose liquidity. Therefore small customers, unable to trade overseas, will be most adversely affected by the loss of liquidity in US markets. Spot markets, such as grains and the US treasury bond market will be adversely affected by the loss of liquidity in futures markets, and spot prices will become more volatile. Finally, customers will lose the freedom of choice they now have to pick either a broker who also trades for his own account, or a broker who trades exclusively for customers.

AN ECONOMIC ANALYSIS OF DUAL TRADING

by

Sanford J. Grossman

Trustee Professor of Finance
The Wharton School
University of Pennsylvania

July 15, 1989

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1. Executive Summary

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Dual trading plays a particularly important role in futures markets as contrasted with securities markets. The fact that all trading in futures takes place on the exchange floor and that spread trading is an important part of hedging strategies make the skills of a trader more necessary for a good futures broker. The immediacy required by the futures market makes liquidity more important, and therefore makes a larger supply of market makers more critical.

There are three types of brokerage services the customer needs. The first service ("search") involves searching for the parties who are interested in being on the other side of the trade (i.e., the contra-party). The second service ("timing") involves obtaining and processing information to determine how long to wait for the arrival of the most advantageous contra-party while being exposed to the risk of an adverse price move. The third service ("bargaining") involves actively bargaining among available contra-parties to obtain the best price.

A securities broker can use his skills and sales force to prearrange trades "upstairs". Upstairs search is often an effective substitute for the downstairs working of an order where "timing" and "bargaining" skills are needed. A futures broker cannot prearrange trades upstairs. The brokerage firm cannot substitute "search" skills for trading skills. The order must be worked on the Exchange floor. The floor broker must have the ability to trade in such a way on the floor of the Exchange that he brings the other side of the trade to the floor at a good price for his customer. Therefore floor trading skills are relatively more important in the futures market than in the securities market.

Further, much futures trading involves "spreads" where a customer wants to buy and sell two (or more) contracts simultaneously for a guaranteed net price. The customer's broker can execute the spread by trading with a "local" on the floor, or the broker can execute the individual "legs" of the spread consecutively. The latter will be in the best interest of his customer if the broker is a skilled trader, since, by trading each leg himself, the broker avoids paying the local a premium for the risk in trading the spread. Such spread trading is inherently risky to a broker, since after he executes one leg of the spread his customer can hold him to a price for the other leg of the spread, which the broker may find impossible to achieve if the price moves after he does the first leg. This aspect of futures trades as well as the relatively higher underlying price volatility in many futures contracts increase the trading skills burden on a futures floor broker relative to that of a securities floor broker.

Futures trading customers often have a high demand for immediacy because they are trading to hedge an underlying spot market position. The fact that immediacy of trade execution is extremely important to futures customers implies that they will have a greater demand for market makers than will be the case in markets where the cost of delayed execution is smaller. A commodity hedger bears great risk if he does not do his futures trade immediately. This risk may force him to trade using a "market" order, for example to sell immediately to the highest bidder currently available. If there are few market makers then he will receive a relatively low price, i.e., his trade will have a high market impact cost. Thus futures markets have a great demand for traders who in effect serve a market making function. The institution of dual trading permits this demand to be met at low cost.

Dual trading increases the supply of the types of customer services which are relatively most demanded by futures customers. Dual trading is prevalent in the securities market, both on the floor and off the trading floor. Institutional securities trades are often prearranged off of the floor, and this lessens the burden of securities floor brokers. It would be quite peculiar to eliminate dual trading for futures and maintain it for securities where the dual trading by floor brokers is less important. The elimination of dual trading from futures markets will harm customers by reducing the quality of brokers who do customer business. The best traders will trade for their own account, leaving customers with brokers who are less skilled traders. By preventing traders from acting as brokers, the elimination of dual trading will reduce the number of floor traders, and thus reduce market liquidity. Foreign markets will gain an advantage over US markets causing large customers to leave US markets which will lose liquidity. Therefore small customers, unable to trade overseas, will be most adversely affected by the loss of liquidity in US markets. Spot markets, such as grains and the US treasury bond market will be adversely affected by the loss of liquidity in futures markets, and spot prices will become more volatile. Finally, customers will lose the freedom of choice they now have to pick either a broker who also trades for his own account, or a broker who trades exclusively for customers.

2. Introduction

Dual trading is said to occur when an entity sometimes trades as a broker for customers, and at other times trades for its own account. This paper explores the economic function of dual trading, and proposes methods for calculating its impact on market liquidity and the quality of customer brokerage services. A later paper will implement those methods on actual trading data.

The structure of this paper is as follows:

Section 3 provides some general background on the organization of markets and trading. It will be seen that dual trading is pervasive in the United States securities and futures markets, though futures markets can be distinguished from securities markets by the fact that dual trading is permitted off the trading floor in securities while it is prohibited for futures. The Appendix provides a summary of the extent to which dual trading exists on markets throughout the world.

Section 4 provides an economic analysis of the determinants of the effectiveness of markets. It examines the demand for, and the supply of various brokerage services. It also explains the determinants of market liquidity.

Section 5 shows how dual trading impacts on the ability of brokers to deliver the above services, and how dual trading impacts on market liquidity.

Section 6 applies the above analysis to determine the likely consequences of eliminating dual trading in futures markets.

Special attention is given to evaluating proposals to selectively eliminate dual trading in particular commodities or contract months.

Section 7 discuses various methods which can be used to compute the monetary benefits to customers from the existence of dual trading.

3. Customer Order Flow and Market Structure

Dual trading can best be understood by tracing the manner in which a customer order is executed. It is convenient to begin with a customer who wants to buy an "item". This item might be a futures contract, a listed security, a government bond, etc.

Discussion of Table I

Table 1 presents the first part of the path which the order can traverse. Part A of the Table analyzes the order flow if the customer gives his order to a dealer, while Part B considers the case where the order goes to a broker. In Part A, the customer deals with a principal, while in Part B, the broker acts as the customer's agent.

Part A1 is the simplest case, where the customer trades directly with the dealer. This type of trade is characteristic of the fixed income market, for example US treasury bonds, municipal bonds, corporate bonds, etc. It is also the method by which the spot and forward market in foreign exchange, and interest rate swaps operate. In such markets, the customer trades directly with a dealer. As will be elaborated in the next section, the customer must engage in active search to find the dealer who is offering him the best price. He is not employing an agent to do the work for him.

Table 1

With Whom Does the Customer Initiate His Trade

A. Customer Uses a Dealer.

A1. The customer can trade directly with a dealer who sells to him from the dealer's inventory.

A2. The customer can trade directly with a dealer who obtains the item elsewhere.

A2a. The dealer could obtain the item from another dealer who has it in its inventory.

A2b. The dealer could obtain the item from another customer.

A2c. The dealer could obtain the item indirectly from another customer by obtaining it from a dealer who obtains it from another customer.

B. The customer can use a broker to find a buyer.

B1. The broker can find a seller on an Exchange.

B2. The broker can find a seller from its own customers.

C. The Customer uses Broker/Dealer Services.

The Broker/Dealer executes its customer's order by selling from its own account and by finding customers who want to sell.

Part A2 considers the case where the customer desires an item which the dealer does not have in his inventory. In such a case the dealer will attempt to obtain the item from another dealer, or from another customer. That is, the dealer is acting like a broker by engaging in efforts to obtain the item for his customer. Therefore even in pure dealer markets, brokerage services are provided. More importantly, it is impossible to distinguish trades made on behalf of a customer from trades made on the "brokers" own account. The broker/dealer almost always trades ahead of his customers in a pure dealer market. The broker/dealer must do so in order to obtain the item for his customer.

Part B of Table 1 considers the case where the customer uses a broker to obtain the item for him. The clearest example of this situation occurs with regard to futures contracts. A customer desiring to trade a futures contract, is prohibited by CFTC regulations from trading directly with a dealer off of the floor of an Exchange. The customer must engage the services of a broker to act as his agent. This is labelled B1 on Table 1.

A more complex situation is summarized by B2, where the broker can find a seller from among its own customers. An important example of this phenomenon occurs in the institutional trading of common stock. A customer who desires to purchase a large block of common stock may ask an NYSE member firm to attempt to find sellers. The member firm will utilize various information sources to locate existing holders of the stock who might be sellers. The member firm will then bring both the buy and sell orders of its customers to the NYSE floor where the orders will be crossed.

Part C of Table 1 considers the case where the customer uses the firm to be simultaneously a broker and a dealer. This was already implicit in the "pure" dealer relationship described in Part A2, but it can be very explicit in the case of securities. Consider the example mentioned above where the NYSE member firm is putting together the purchase of a large block of stock for a customer. If the broker/dealer cannot find enough customers who want to sell, it might sell out of its own inventory, and thus takes part of the other side of its own customer's trade. It would then bring the whole trade to the NYSE floor for open outcry.

The above remarks indicate that securities are traded by firms that engage in a type of dual trading which I will refer to as simultaneous dual trading. That is, the firms are being both brokers and dealers at the same time for the same customer. It may be useful to contrast this with what I will call consecutive dual trading in which the firm sometimes trades as principal and sometimes trades as agent, but does not do both in a single transaction. Simultaneous dual trading occurs in the securities markets (including options) but does not occur in the futures markets.

A customer in the securities or futures industry will use a firm which does one or the other of the above types of dual trading. The economics of why this is the case will be analyzed in the next two Sections. Here it suffices to note that just about every firm which accepts customer orders also trades for its own account; there are very few firms that trade only for their own account, or that trade only for customers. This is literally true in the dealer markets like the fixed income markets and the over the counter stock market (where the distinction between principal and agent trades does not exit), but it is also true for common stock and futures contracts.

Discussion of Table 2

Table 2 traces the next step followed by the customer's order under the assumption that it is not executed directly by the broker/dealer accepting the order. In particular, the order is traced through its execution on an Exchange. It is convenient to refer to the broker who first receives the customer order as the "upstairs broker". It is conceptually useful (and usually descriptively accurate) to visualize the upstairs broker transmitting the order "downstairs" to the trading floor of an Exchange, or transmitting it to a computerized "Exchange" (such as the NASDAQ "over the counter", or Instanet "markets"). The recipient of the order on the Exchange floor can be a pure "agent" on the Exchange floor who never trades as a principal (category A on Table 2), or it can be a floor broker who does both customer business and also trades for his own account as a principal (category B on Table 2).

Table 2

Tracing the Customer's Order On An Exchange

A. Customer's order handled by an AGENT on the Exchange floor.

A.1 Employee of the Exchange executes the customer's order.

A.2 Floor broker who specializes in trading for customers executes the customer's order.

B. Customer's order handled by a PRINCIPAL/AGENT on the Exchange floor.

B1. A broker/dealer handles the order.

- B1a. The broker/dealer handles it as an agent.
- B1b. The broker/dealer handles it as an agent and principal.

B2. A broker/trader handles the order as an agent.

B3. A broker/market maker handles the order.

- B3a. He handles it as an agent.
- B3b. He handles it as a principal.

The purest form of an "agent" who executes the customer's order on the Exchange floor is an employee of the Exchange who executes customer orders (category A1 in Table 2). This occurs on many foreign Exchanges (such as the Tokyo Stock Exchange), as well as on the Chicago Board Options Exchange (CBOE) where an Exchange employee maintains a limit order book for customer orders, and handles the execution of these orders when the market price reaches the level at which the customer indicated that he is interested in trading. Note that by "executing the customer order", I do not mean that he takes the other side of the trade. Rather, the agent follows the prescribed rules of the Exchange in an attempt to get the best price for the customer. This may involve announcing to the trading crowd that he has an order to fill, and then trading with the member of the trading crowd who offers the best price. The member of the trading crowd with whom the agent trades may himself be representing customers as an agent or he could be trading for himself as a principal.

Part A2 of Table 2 indicates a less extreme situation where a member of the Exchange decides to specialize in trading for customers on the floor, and essentially does no trading as a principal for its own account. Almost all Exchanges have individual members who have built a reputation as good brokers trading for customers, but who do little or no trading on their own account.

In contrast to the above situations where the customer order is handled by "agents", an enormous amount of floor brokerage is effected by firms that are broker/dealers, broker traders, or broker/market makers. These categories appear in Section B of Table 2. An example of category B1 is a broker/dealer such as Merrill Lynch who handles a customer's stock trade on the NYSE Exchange floor. The Merrill broker can act as a pure agent (category B1a on Table 2) who buys the stock on the Exchange from another broker in an open outcry auction. In a more complex case, Merrill may be both a principal and an agent; selling to the customer partially from its own account and partially for other Merrill customers. For large institutional trades, the Merrill floor broker may be representing Merrill Lynch, and both buying and selling customers on the NYSE floor at the same time in the same trade. Merrill negotiates the trade secretly upstairs, and exposes the orders "downstairs" on the trading floor by offering out one side of the trade to whomever is present at the specialist post.

Categories B1a, and B1b indicate that the broker dealer may handle the order as an agent (not taking a part of the trade on its own account), or in contrast as in the above example, the firm may be acting simultaneously as a principal and an agent in executing the customer's order. In the situation where the broker/dealer acts as both a principal and an agent, it is engaging in what I call simultaneous dual trading. In the case where it executes this customer's order as an agent, it may be engaging in consecutive dual trading, since at some other time it may be trading in the stock as a principal.

In order to further emphasize the distinction between these types of dual trading, Table 2 contains the additional category, B2 of "broker/trader". A broker/trader is a floor trader who sometimes trades on his own account as principal, and at other times trades as a broker for customers. He is not a "dealer" in that he does not take the other side of customer trades. He is a consecutive dual trader but not a simultaneous dual trader. As noted earlier, consecutive dual trading is permitted on futures markets, but simultaneous dual trading is not permitted. In contrast, both types of dual trading occur on the floor of securities Exchanges.

The final category of Table 2, labelled B3, concerns the situation where a designated market maker handles the customer order. For example, on the NYSE, the upstairs broker may give the "specialist" (who is a broker's broker, and a market maker on the NYSE floor) a customer order. The specialist may handle this order as an agent and find the other side of the trade among other floor brokers (category B3a in Table 2). On the other hand, the specialist may act as a principal, and take the other side of the trade on its own account. Thus the specialist can engage in simultaneous dual trading.

Summary

A customer's order for securities or futures will usually be handled by firms engaged in dual trading. This is the case at the "upstairs" level where the customer order arrives at a securities broker/dealer or Futures Commission Merchant (FCM), each of whom trades for its own account as well as for customers. However, it is also the case at the "downstairs" level on the trading floor where the customer's order is handled by a specialist, broker/dealer, or broker/trader, each of whom engages in some form of dual trading.

It should not be surprising that firms which develop facilities for trading on their own account will also be able to provide high quality executions for customers. In the next Section, I explain why it is the case that good executions of customer orders often involve substantial trading skills.

4. The Determinants of Market Liquidity and Brokerage Services

4A. Brokerage Services

Consider a customer who desires to trade. He may desire "dealer" and/or "brokerage" services. We will see below that it can sometimes be difficult to distinguish dealer from brokerage services. There are three types of "brokerage" services the customer needs. The first service ("search") involves searching for the parties who are interested in being on the other side of the trade (i.e., the contra-party). The second service ("timing") involves obtaining and processing information to determine how long to wait for the arrival of the most advantageous contra-party while being exposed to the risk of an adverse price move. The third service ("bargaining") involves actively bargaining among available contra-parties to obtain the best price.

The above three activities (or services) are performed in obvious ways in some markets, but in a subtle manner in other markets. For example, the sale of a house often requires the use of a broker who advertises the house and searches for buyers. The owner of the house must decide whether to accept the first offer he receives or delay the sale until other potential buyers (hopefully willing to pay more than the current buyer) are found. Finally, the seller must bargain among the buyers to try to obtain the highest price.

Brokerage Services For Institutional Securities Customers

The institutional securities market provides another example of brokerage services. A portfolio manager may desire to hedge his portfolio of stocks buy purchasing put options. He might want 10,000 SPX index options. These options trade on the CBOE, and the typical trading volume in the particular option of interest might be 1,000 options per day, and the quotation on the option may show 100 options offered at $3.00 per option. The portfolio manager will call the index products department of a broker/dealer. The broker will call its trader on the Exchange floor to ascertain at what price 10,000 options can be purchased on the floor. Typically, the price will be higher than the $3.00 shown on the quotation screen at which only 100 options were offered for sale. At this point, the broker will use its knowledge of its other customers' trading desires to search for a better price than is being offered on the floor. It may find customers willing to sell 9,000 options at $3.00. It may then "accommodate" the customer by selling 900 options from its own account. The broker will then bring the order down to the floor of the CBOE and bid for 10,000 options for a price of $3.00. Assuming that the crowd on the trading floor is still only offering 100 options, the broker will sell 900 from its own account, and 9,000 from its other customers, effectively crossing the order on the Exchange floor. Note that the broker engaged in a dealer function in order to better provide brokerage services to its customer.

It should be emphasized that the "search" function is intimately related to the "timing" function. The customer is subject to the risk that the market will move against him while he tries to get a better price than is currently offered on the Exchange for the large number of options which he is attempting to buy. He also bears this risk, if he and the broker engage in bargaining to attempt to get a higher price. It is crucial that his broker have a "feel" for the potential price movements, and also knowledge about the prices at which his own customers are willing to sell. If the broker acts as a dealer by selling some options from his own account to accommodate the customer, then he must also have the same kinds of knowledge and ability. To summarize, the institutional brokerage function will be performed most effectively by a firm with the skills and knowledge of a trader. For trades which cannot simply be sent to the Exchange for immediate execution (i.e., as a "market" order), the broker is not merely a clerk. He must engage in all of the activities, and have all of the skills of a trader.

The search function is even more important for the market in individual common stock. A buyer of a large block of common stock must often find sellers off of the Exchange floor. Here again the information brokers have about sellers will be crucial. First, the brokers can review public documents which provide the names of large institutional holders of the stock. The broker can then solicit selling interest from them. Second, the brokerage firm can call upon the knowledge of its sales force which stays in day-to-day contact with investors, and thus comes to know something about who is willing to sell and at what price.

In the securities market a broker can directly contact potential trading partners who are not present on the Exchange floor and he is thereby able to gain information for his customer about the costs and benefits of delay. The fact that it is possible and necessary to gain off-floor information distinguishes the activities and necessary skills of securities brokers, from futures brokers. Though any floor broker can communicate with his upstairs office, futures markets are distinguished from securities markets by the fact that price discovery occurs exclusively on the trading floor for futures, while price discovery occurs upstairs as well as downstairs in the securities market. Unlike securities brokers, futures brokers cannot secretly prearrange trades upstairs, and thus the futures floor broker must trade in such a way as to bring the other side down to the trading floor, as is analyzed below.

Brokerage Services for Futures Customers.

Consider a grain storage firm which desires to hedge its position. The broker who receives this order will transmit it to the futures Exchange. He is prohibited by regulations from working the order "upstairs". The broker who executes the trade on the trading floor must carry the full burden of "search", "timing", and "bargaining". For example, if the order is to sell 3 million bushels at a time when only 100,000 bushels are being bid for $3.00, then the floor broker must trade in such a way that he induces buyers who may be "upstairs" to send orders to the floor. This is an implicit form of "search". The broker could simply announce that he has 3 million to sell, and hope that the other floor brokers will call potential customers "upstairs" to induce buying. However, unlike securities, commodity futures brokers may have less information about their customers underlying interest in particular positions. This information is often proprietary and strongly related to the underlying business operation of the commodities customer. Thus, the only effect of announcing that he has 3 million bushels to sell will be to cause a large fall in price which will give the customer a poor (if any) execution.

The situation is further complicated by the fact that the customer may be bearing extreme risk while the broker delays the execution of the trade in an attempt to get a better price. The fact that futures customers are often hedging underlying commodity or securities positions means that they can face greater risk from delayed executions than a securities customer. In the above example, the grain storage firm's overall profitability will suffer greatly if grain prices fall before it can hedge its inventory.

The floor broker can sell some futures, perhaps driving the price down a little. The fall in price communicates "through prices" that the market needs buyers. The prices at which trades occur on the Exchange are communicated to the world. A customer (off of the Exchange floor) who was not interested in buying at the previous price may become interested in buying after seeing trades at lower prices. The floor broker is thus using his trading to indirectly communicate with potential customers who are off of the trading floor. This is an alternative mechanism to that which occurs in the trading of securities where much communication occurs upstairs on the telephone between brokers and their customers.

The futures broker attempting to sell 3 million bushels will sometimes find it necessary to disguise the true intention and size of his order. No buyer wants to buy from the broker just before the broker sells 2 million bushels. A broker who keeps selling in an attempt to generate buying interest can actually cause buying interest to disappear. For this reason a broker may find it advantageous to occasional intersperse his customer sell orders with buy orders for his personal account. This helps disguise his intentions. The effective execution of the customer order involves a subtle interplay between communicating a desire to sell in an attempt to attract buyers, while disguising the full size of the order.

The floor broker on the futures market can only bargain with those present on the floor. At each stage of the execution of his customer's order he can accept the bids currently being made, or he can make a counter-offer. He bargains through open outcry with the trading crowd on the Exchange floor. This is in contrast with the securities market, where a floor broker can seek better bids "upstairs".

The above remarks indicate that the floor broker on the futures market must have all of skills of a good trader in order to give his customer a high quality execution. A person who trades for his own account on the Exchange floor makes money by being able to judge where the market is going to move in the short run. A floor broker's greatest fear is that the market will move away from him (for example, that the existing bids will disappear and be replaced by lower bids) while he delays execution of his customer's order in an attempt to get him a better price. The ability to judge short run market movements is thus at the essence of being a good floor broker and being a good trader.

Summary

The distinct characteristics of a futures market imply that a futures broker must behave like, and have all the skills of a trader. This is much more the case than in securities markets where a broker can effect a good execution for his customer by the use of a its upstairs sales force which brings both sides of the trade together. The key skills if the floor trader are "timing" and "bargaining" - these are used in place of upstairs "search" to obtain a contra party for his customer at the best price.

4B. The Determinants of Market Liquidity

The quality of brokerage services is only one of the determinants of the quality of order execution. A customer can have an excellent broker, but if the market in which the broker executes the trade is illiquid, then it will be very difficult to get a good execution. Therefore an understanding of the quality of customer order execution requires an understanding of the determinants of market liquidity.

Clearly, markets serve the function of enabling parties to engage in trade. However this is not the only function of markets. Markets serve a price discovery function: providing and aggregating information across both active and inactive market participants.

These points can be clarified by temporarily making the following artificial distinctions. Divide the potential market participants into three groups: brokers, market makers and final customers. Pure brokers are agents, who by definition, never take a position in the instrument being traded, and I have discussed them extensively in the previous section. Market makers, by definition, take a position only for short term trading profits, i.e., the average return from a position held for the long run will not reward them for the risk of capital committed over the long run relative to other uses they have for their capital. Final customers, by definition, are willing to accept the average returns for the risk of their positions over the long run, and are trading perhaps with great current immediacy to achieve that position. This division of actors is obviously artificial, but it will help to explain some important concepts.[1]

Final Customers

The final customer could be a bond dealer who sells bond futures to hedge a portfolio of bonds in its inventory. The customer faces the risk that bond prices will fall before he is able to sell the bonds in his inventory. He insures against this risk by selling bond futures. He bears the risk of a price fall while his broker attempts to fill his order on the Exchange floor. This customer may be willing to accept no return on average from being short the bond future. He is willing to take a zero or even negative expected return position because of the insurance provided by the position. In particular, if bond prices rise, then his losses on the bond futures are offset by gains on the bond inventory.

In the securities market, the final customer might be a money manager who wants to add a particular industry group to its portfolio of common stock. This type of customer demands less immediacy of order execution than does the futures customer who is trading to hedge a position. The money manager does not hold a large group of assets that are necessarily going to enjoy a price move in the opposite direction from the price move in the stocks that are being purchased. Though there may be some diversification effect leading to a risk reduction from a securities trade, it tends to be much smaller than the risk reduction effected by a commodity futures hedge.

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[1] See Sanford Grossman and Merton Miller, "Liquidity and Market Structure," The Journal of Finance, July 1988, Vol. 43, No. 3, p.617-37.

Market Makers

The market maker could be a dealer buying at a price from which it expects high abnormal returns. The market maker buys the instrument in situations when the price is temporarily low, while the final customer buys the instrument because (a) the long run average return is high relative to its risk, or (b) the reduction in risk of his overall portfolio compensates for the low expected return of buying the instrument. More precisely, the market maker takes positions because of the variability in the expected return (buying when expected returns are high and selling when expected returns are low), while the final customer takes positions based upon the long run average expected return. Many trading institutions who are usually final customers in the above definition, will function as market makers when there are clear variations in expected returns. For example an S&P 500 Index Fund may substitute futures for stock when futures are trading at a discount relative to stock. The fund is taking a position in the spread because the spread has a temporarily high (risk adjusted) expected return.

To better understand the role of market makers, consider the following example. For reasons unrelated to information about future payoffs, a group of equity holders desires to sell a substantial block of equity. Assume that a negligible price fall would be required to induce the rest of the economy to increase its equity holding by the amount that is to be sold. That is, if final buyers could be matched with final sellers, then there would be no price impact of the trade. However, the potential final buyers are dispersed throughout the economy (if not the world), and are not in constant communication with the market. A market maker will buy the offered stock into his inventory to bridge the time interval between the arrival of the sellers and buyers. He bears risk while the stock is in his inventory, and hence must, on average enjoy a reward.

A market maker (or final customer, behaving like a market maker) buys when expected returns are high (relative to the normal risk adjusted return for the asset), and sells when expected returns are low. A large unanticipated flow of sell orders which occurs in the absence of information about future payoffs, will lower price and raise expected returns (in the absence of market maker intervention). It is the fall in price, in the absence of news, which signals to the market makers (and eventually the final buyers) that their intervention is necessary. The price move is a crucial signal for allocating resources. The buying activity of market makers trying to take advantage of the high expected returns will diminish the size of the price fall, and thus stabilize the market.

Market makers engage in exactly the same activities in the futures market. The only important distinction for our purposes is that the activity only occurs on the Exchange trading floor in the case of futures, while it can also occur off of the Exchange floor in the case of securities. Therefore the market makers on the floor of a futures Exchange are the only source of liquidity for a futures customer, while there are also off-floor sources of liquidity for securities customers.

Markets as Information Conveyors

The ideal market would be one in which everyone in the economy could costlessly, effortlessly, and continuously participate. In such an ideal market there would be no brokers (and they surely would disagree with this definition of ideal), because there would be no search for contra-parties. There would also be no market makers, since no one is needed to bridge the gap in time between the arrival of buyers and sellers at the market; all potential buyers and sellers are always costlessly and effortlessly present. Unfortunately, discussions of ideal markets can be sterile, as I feel are discussions about ideal worlds without wars, earthquakes, bad weather, or government regulators.

A major factor which causes markets to deviate from the ideal is the fact that continuous participation and information retrieval and evaluation is neither effortless nor costless. If one party wants to sell, this information is not costlessly disseminated to, and processed by all potential buyers. More importantly no single person is being made aware of the collective demand and supply schedules of the rest of the market.

The fact that we are not all part of this fantastic, telepathic network creates the need for information to be provided by markets and broker/dealers, as well as the need for market makers.

Market makers take a position in the instrument, and bridge the gap in time between the arrival of the final sellers and buyers. In the absence of a large supply of market makers, a customer order will have a large "market impact" cost of execution. This cost is the fall in price caused by a sellers demand for immediate order execution, and the rise in price caused by a buyers demand for immediate order execution.

The market impact of a trade clearly depends on how the trade is executed. There are two reasons for this. First, orders which demand immediate execution convey information to other participants. Market participants know that one reason that a trader demands immediate execution is that he has information, they thus offer to trade at adverse prices with the trader who demands immediacy. Of course, immediacy may be demanded for other reasons, such as a liquidity or hedging need. The weight put on the information motivation for the trade will determine the size of the market impact of the trade. The market impact of a trade depends on the method by which it is executed for a second reason, namely if a final customer is not present to take the other side of the trade, then someone must earn a return from taking the other side of the order into his inventory. This return is to cover the risks and other costs of maintaining an inventory, and the market maker earns this return by taking the other side of the trade at an adverse price to the customer. This adverse price move is the market impact of the trade.

The greater are the number of market makers, the smaller will be the market impact of a given customer order. The impact is smaller not only because of the increased competition, but also because each market maker can take a smaller fraction of the customer's order into his inventory when there are more market makers. The smaller is the position that a market maker is asked to take, the more willing he is to trade at a price which does not disadvantage the customer (for example., a market maker will be willing to buy at a higher price, the less he is asked to buy, since he has a smaller inventory and thus less risk).

The number of market makers available to take the other side of a customers trade will be determined by the costs and benefits of market maker activities. The costs of market making involve
(a) the cost of capital to carry (or margin) positions;
(b) the costs of training;
(c) the cost of the time spent on the trading floor.
Anything which reduces the cost of market making will raise market liquidity, and lower the market impact cost to customers of effecting their trades.

Summary

The quality of execution available to a customer will depend on the quality of the brokerage services provided to him as well as the underlying liquidity of the market in which he trades. The floor brokerage services needed by a futures customer involve the broker in the use of trading techniques which only a skilled trader will have mastered. The (1) inability to prearrange trades "upstairs" for futures customers and (2) the great demand for immediacy inherent in a hedge transaction, imply that floor trading skills are relatively more important to the typical futures customer than to the typical securities customer. Further, the above two characteristics of futures trading also imply that the liquidity of the Exchange floor will be relatively more important for futures than for securities customers. Anything which can reduce the cost of market making will thus tend to be relatively very important for achieving quality futures trade executions for customers.

5. Dual Trading, Market Liquidity, and the Quality of Brokerage

The economics of brokerage services and market liquidity outlined in Section 4 provide the basis for understanding the pervasiveness of dual trading discussed in Section 3.

The previous discussion showed that the skills of timing and bargaining are important both for the broker in getting the best execution for his customer and for a market maker trading for his own account. It should be added that a broker who trades for customers bears risk. This risk occurs because he agrees to execute limit orders, spread orders, and stop loss orders for customers. If he fails to execute these orders as agreed then he will have to make up the losses to his customer.[1] The institution of dual trading permits an individual to use his time, skills and risk bearing capacity for two activities, namely market making and customer brokerage. In order to engage in trading, a person must bear the costs of training, an Exchange seat, and the time spent on the trading floor. A system in which the trader can earn a return from these costs by spreading his talent and energies over two activities will clearly encourage more people to be engaged in the activities. Thus the institution of dual trading increases both the supply of market makers and of brokers.

Therefore dual trading has both a direct and an indirect effect on the quality of customer services. The direct effect is that it increases the pool of brokers available to customers who are skilled at providing the services of search, timing, and bargaining. The indirect effect is that it increases the supply of market makers, so that even if the customer's order is not executed by a dual trader, his broker will be able to provide the above services at lower cost because of the increased liquidity provided by the increased number of market makers.

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[1] For example, if the broker accepted a limit order to buy at a price of $3 or below, and a trade occurs at $2.90 afterwards, and then all trades occur at prices above $3.00, then the broker will be held accountable by his customer for a price between $2.90 and $3.00.

The Importance of Dual Trading in Futures Markets

Dual trading has a particularly important function in futures markets in the United States for three reasons. First, various regulations make the Exchange floor of the futures market the only focal point of trade. Second, the nature of many types of futures trades would make it very difficult to search for contra-parties "upstairs", even if such activities were permitted. Finally, the high degree of immediacy demanded by many futures customers both increases the advantages of using a skilled floor trader as a broker, and also the advantages of having a liquid market on the Exchange floor. These points are elaborated upon below.

The Exchange Floor is a Focal Point In Futures Markets

It is a violation of CFTC regulations for trades to be arranged off of the trading floor. Hence the only source of liquidity to customers is the liquidity provided on the Exchange floor. This should be distinguished from the situation which prevails in securities markets. A securities customer who, for example, wants to sell a large block of stock can use the services of "upstairs" brokers to search for buyers off of the Exchange floor. Eventually, the broker will find buyers and possibly commit its own capital as a buyer, and bring the trade down to the floor of the stock Exchange to be crossed. The "upstairs" securities broker is able to search for buyers without revealing to the world how much its customer is interested in selling. Further, he can provide information to his customer regarding what price can be obtained for the block. In a futures market this type of information can only be obtained by careful trading. There is a greater burden put on futures floor brokers than is put on securities floor brokers. Performing the tasks of timing and bargaining are more difficult on futures markets than on securities markets because the absence of upstairs search places all the burden on floor brokers. In particular, the futures broker must extract information through his trading that would have been extracted by the securities broker through telephone calls.

Another important consequence of the fact that the futures pit is the focal point of trade is that potential buyers and sellers do not have to search among upstairs brokers for the best price; they need only look to the trading floor. Though a futures floor broker must work hard to communicate his clients need to the world through trading, this has the effect of enhancing the value to the world of the observed prices at which trades occur on the futures floor, i.e., price discovery takes place on the trading floor. This is in contrast to the securities market where much institutional price discovery takes place in secret upstairs. If a trade is negotiated upstairs, then this is done in secret, and the rest of the world is not informed until the trade is brought down to the Exchange floor to be crossed.

The fact that futures markets put a heavy burden on floor brokers means that there is a greater need for skilled floor traders in such markets. The skills needed by a floor broker are very similar to the skills needed by someone trading for his own account. The ability to sometimes work as a broker and other times work as a trader increases the rewards that a skilled trader can earn, and hence increases the number of such traders present on the Exchange floor.

It should be emphasized that the CFTC regulations prohibiting "upstairs" trading are not the only reason that a futures Exchange tends to be more of a focal point of trade than is the case for a stock Exchange. The fact that a futures customer's hedging needs are intimately related to secret aspects of its business will make it relatively more difficult for brokers to know where to find contra-parties to a futures trade, than it is to find contra-parties to a securities trade. A grain exporter who has just signed an agreement to deliver wheat to a foreign country, and may thus have a great desire to have a long futures position, will not tend to publicize this fact. This is in contrast to a money manager who desires to add an industry group to its portfolio over the next few weeks. The latter is likely to be revealed to securities brokers. Thus it is more likely that securities brokers know where to look for the "buy" side of the trade in the above securities example, than that they could discover that the grain exporter is a potential buyer in the commodity example. The contrast is even more extreme when a broker needs to find the sell side. In the case of common stock, the broker can find all large institutional holders of the stock (from form 13F filling made with the SEC) and solicit a sale from them. No corresponding holders of short commodity positions need exist. The very fact that there are "shares outstanding" of equities is in contrast to futures where "short" and "long" positions must be created by customers. The existence of the shares outstanding creates shareholders (i.e., potential sellers) who can be directly contacted by brokers, in contrast to futures where all potential creators of "short" positions would have to be contacted in an attempt to find a seller.

Futures Customers Require Brokers Who are Traders

Many futures orders are for "spread" trades. A spread trade involves selling one contract and buying another contract. For example a customer currently holding a short Treasury bond contract for June expiration may want to buy the June contract and simultaneously sell the September contract, i.e., he wants to buy the June/September spread. This type of trade is very common because, unlike common stock, futures contracts expire. A customer who wants to maintain his hedged position must "roll" his position into the next contract month (by trading out of his position in the contract which is about to expire, and simultaneously trading into the same position in a contract with a later expiration). Note that the customer will give the order to the broker as a single spread trade, rather than as two separate trades because the customer does not want to bear the risk of a price move while only one "leg" of the trade is being executed.

The customer's broker has two choices in executing a spread trade. He can trade with a market maker who sells him the spread at a specified price, or he can "leg" the trade himself by, for example, selling the September contract first, and then waiting for a propitious time to buy the June contract. For example, suppose the customer gave him the order to buy the spread for 3/32 which means to pay 3/32 more for the June contract than he receives from selling the September contract. There may be a market maker on the floor who is willing to sell the spread for 3/32. However, the customer's broker sees that the June contract is being offered at 96-07, and the September contract is bid for 96-04 and offered at 96-06.[3] So he decides to buy the June for 96-07 immediately, and offer the September at 96-05, with the hope of saving his customer 1/32. If he is right in his judgment of the market then he will be able to sell the September at 96-05, but if he is wrong then he may have to sell at 96-04 or below. If the market moves against him before he can sell the September at 96-04, then he will have to pay his customer for the difference between 96-04 and the price he executes the trade.

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[3] Note that 96-06 means 96 and 6/32.

Spread trading is inherently risky.[4] A good broker is a trader skilled at taking the types of risk described above. This very specialized trading skill is used by a dual trader to trade for his own account with the brokers for other customers who do not want the risks, or to trade for his own customers. A particular spread trader may go through periods where he has no customer business, but is able to support himself by trading for his own account. When his customers need him he is able to stop trading for his own account and provide them with spread brokerage services. The institution of dual trading thus puts more spread traders on the Exchange floor than would otherwise be present because it gives each trader more business in which he can earn a return from his skills, for the time he spends on the floor, and for the cost of his Exchange membership. It also permits the broker to use his risk bearing capacity to both cover the risk of trading on his own account as a market maker, and also the risk of being unable to fill customer limit and stop-loss orders.

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[4] A broker can avoid this risk by trading the spread directly with a local, however then the customer is indirectly paying someone else to bear the risk, and in effect using two people to execute the trade rather than one person.

Dual Trading and Liquidity on Futures Markets.

The above remarks indicate that customers will receive more skilled brokerage because of dual trading. However, there is an indirect benefit to customers from dual trading which they receive even if they use a broker who never dual trades. This benefit is the fact that dual trading will increase the number of market makers and especially spread market makers. The number of market makers is increased from dual trading for exactly the same reason that it increases the number of skilled brokers. The ability to engage in customer brokerage enhances the value of an Exchange membership to a market maker. The market maker knows that after he has committed as much of his own capital that he can to trading on his own account, then there is still another way to earn income from his presence on the trading floor, namely customer brokerage. This "second income" can be a substantial inducement to be a market maker, which significantly lowers the effective cost.

The fact that immediacy of trade execution is extremely important to futures customers implies that they will have a greater demand for market makers than will be the case in markets where the cost of delayed execution is smaller. A commodity hedger bears great risk if he does not do his futures trade immediately. This risk may force him to trade using a "market" order, for example to sell immediately to the highest bidder currently available. If there are few market makers then he will receive a relatively low price, i.e., his trade will have a high market impact cost. Thus futures markets have a great demand for market makers who accommodate immediacy of order execution. The institution of dual trading permits this demand to be met at low cost.

There is also great variability in the customer demand for both brokerage and market making services. The variability in price volatility which is common in futures markets creates both a great need for reserve brokerage capacity (as seen, for example, in the summer of 1988 where grain price volatility and trading volume rose after some slow years) and produces lulls during which it is hard for non-dual trading brokers to survive.

6. Preliminary Evaluation of Proposals to Restrict Dual Trading

A. Consequences of Eliminating Dual Trading

The fact that a broker trades for his own account and also trades for customers is a potential source of a conflict of interest. One major conflict of interest is that the broker may "front run" his customer order by trading on his own account before executing the customer's order. For example, a broker holding a large sell order for a customer might sell out of his own account first and thereby benefit from the price fall caused by the execution of the customer order. This potential abuse exists in both the securities markets and futures markets. It is a violation of NYSE rules for a member to trade ahead of its customer, and it is also a violation of CFTC regulations for a futures broker to trade ahead of its customer.

Though the elimination of dual trading may reduce the above conflict of interest, it will actually increase another type of conflict of interest. Front running is not the only source of conflict of interest between a broker and a customer. The broker gets paid for getting the trade executed. The customer wants an execution at a good price. The faster the broker can get the order executed, the sooner he can begin executing the next customer's order and earn another commission. The fact that a customer wants the broker to expend both time and effort to do the trade conflicts with the fact that the broker gets a commission on a particular trade independently of how hard he works the order. (Of course, the customer will not give repeat business to a broker who he knows provides him, with poor executions.) This conflict of interest is mitigated for a skilled broker/trader because it is easier for him to give his customer a good execution. It is also mitigated when there are many brokers (each, not overburdened with orders to be executed), and when a large supply of market makers are available giving good bids for large size orders.

Thus, the first consequence of eliminating dual trading will be to exacerbate the conflict of interest between a broker and his customer. We will show below that the elimination of dual trading will decrease the number of brokers, decrease the number of market makers, and decrease market liquidity. In times of heavy demand by customers for broker services, there will therefore be fewer brokers to handle the customer orders, and each order will be more difficult to execute because of the decrease in market liquidity. Since heavy demand by customers for brokers often occurs at the same time that market volatility rises, the elimination of dual trading will cause there to be: (a) fewer brokers to satisfy the increased demand for brokers, and (b) fewer locals trading as market makers to counteract the increased volatility. Broker/traders who are very skilled at trading will trade for their own account, while broker/traders who are somewhat less skilled will trade only for customers. In periods of heavy customer trading, these less skilled brokers will necessarily be under great pressure to quickly trade each order so that they can move on to the next order, thus maximizing their total commission.

The analysis presented in Section 6 showed that there are four main benefits associated with dual trading:

(1) Customers receive brokerage services from skilled traders.

(2) The number of brokers is increased.

(3) The number of market makers is increased.

(4) The liquidity of the market is increased.

In addition to exacerbating the conflict of interest between brokers and customers, the elimination of dual trading will clearly lower all of the above benefits.

The Best Traders Will Not Do Customer Trades

The best traders are those individuals who have a comparative advantage at judging short run market moves. If these individuals must choose between executing customer trades or their own trades exclusively, then they will choose to trade for themselves. The most that a broker can make from a customer trade is the commission. If he is a good trader for customers, then he will get more commission business, but he cannot share in the profit from individual trades. The most skilled traders will not give up the unlimited profit from buying low and selling high which they obtain from their own trading, in order to get commissions from customers. These trading profits are often high on the same days when there is high price volatility and thus high demand by customers for skilled brokers.

We noted in Section 5 that the facts that futures trading is focused on the Exchange floor and that futures customers often desire spread trades and trades characterized by great need for immediacy all combine to make a futures customer need relatively more skilled floor brokerage services than a securities customer. The elimination of dual trading from futures markets, while the maintenance of dual trading on securities markets would be eliminating the skilled floor brokers from the customers who have relatively the greatest need for their services.

The Number of Market Makers and of Brokers Will Decrease

The fact that an individual can engage in two activities to earn a return for the cost of an Exchange seat, the expenses of training, and the time spent on the Exchange floor will inevitably increase the supply of individuals who are broker/traders. Eliminating dual trading will lower the value of being on the floor for both activities. This is because an individual who now concentrates on being a broker can trade on his own account when his own brokerage business is light, and an individual who specializes in trading on his own account can switch to customer business when customers demand heavy brokerage services or when he has committed all of his capital to trading on his own account.

Dual trading creates a reserve group of potential brokers who can freely switch to customer business when the volume of customer orders rises. It also creates a reserve group of market makers who can add liquidity when customer orders threaten to have a large market impact.

Market Liquidity Will Be Reduced

The elimination of dual trading will reduce the risk capital made available by floor traders who act as market makers. This will increase bid ask spreads. It will decrease the liquidity provided in the periods when it is needed most, namely when there is an unanticipated inflow of customer orders. The inability of brokers to switch from customer business to trading for their own account will prevent them from taking the other side of the large inflow of orders. Therefore price movements will be exacerbated. Market prices will show greater volatility.

Spot Markets Will Be Adversely Affected

The decreased liquidity and increased volatility of futures prices will adversely effect the underlying spot markets. Futures markets serve a hedging and price discovery function which will be impaired by the elimination of dual trading. This will make holding the spot commodity or financial instrument more risky. This will impact on a whole range of underlying activities from grain storage to the financing of the US treasury debt.

One example of the type of impact can be seen in the grain market. Grain elevators buy grain and store it. They bear the risk that the price will fall between the time they buy the grain and the time they sell the grain. The elevator owner can hedge this risk by selling the grain forward on the futures market. He thereby shifts the risk to the rest of the world, rather than bearing it all by himself. The fact that the grain elevator does not have to bear the risk of price fluctuations means that it is able to pay farmers more for the grain. If the elevator owner had to bear the risk of price fluctuation, then he would pay the farmer less, so as to cover the risk he bears in storing the grain. If the liquidity of futures markets falls, or if transactions costs rise, then the effective cost of obtaining insurance from futures markets will rise. This increased cost will be passed along to farmers in the form of a lower price they receive for their grain. Final users of grain will not receive a lower price, but may even have to pay a higher price, since the grain elevator's effective cost of storing the grain has risen due to the increase in its cost of obtaining insurance in the futures market.

Another example of the deleterious effects of reducing futures market liquidity can be seen in the US treasury security market. Bond dealers who put in bids at US treasury auctions can hedge the inventory of bonds they acquire by using the US treasury bond futures market. The ability to hedge their inventory increases the amount that they are able to buy at auctions, and the price that they are willing to pay. If the cost of trading on the futures market rises, then this will increase the cost to the US treasury of issuing treasury securities.

The enormous importance of futures markets in our economy means that even small increases in the cost of using the markets or the liquidity provided by the markets can have very large impacts on the economy. If farmers receive $.05 less per bushel, or if consumers must pay $.05 more per bushel, or, if the US treasury receives 1/32 less per $100 of bonds it issues, then the consequences per 100 million bushels and per 1 trillion dollars of debt are enormous.

Foreign Markets Will Replace US Markets

The fact that dual trading is permitted in many foreign markets will give those markets an advantage over the US markets. The preeminence of many US futures markets arises from the great liquidity added by "locals", who are traders risking their own capital to add liquidity to markets. These locals will lose an important source of their potential income if they are excluded from customer brokerage, and hence be discouraged from entering the trading business.

The movement of brokerage business overseas will further decrease the liquidity of US markets because there will be fewer customers for a given customer on the US market to trade with. Customers forced to trade in the US will therefore be trading in less liquid markets, after mobile customers take their business elsewhere.

Customers Will Lose Their Freedom Of Choice

Currently, with dual trading permitted, a customer concerned about conflicts of interest can choose to use a floor broker who does not engage in dual trading. On the other hand, a customer who is not concerned about the conflict of interest and wants an active skilled trader can choose a floor broker who does engage in dual trading. This freedom of choice will be lost to customers if dual trading is banned.

B. Review of Proposals to Partially Eliminate Dual Trading

1. Eliminate Dual Trading in Liquid Contracts

There are two problems with this proposal. First, the contracts may be liquid exactly because of the ability of broker/traders to switch to market making activities when there is a large customer order which would otherwise have a large adverse price impact. It is very difficult to maintain a liquid futures market. Most contracts which have been introduced by Exchanges fail to become liquid and disappear. No customer will initiate a position when he fears that the market will not be liquid when he wants to take off the position. If customers lose confidence in the liquidity of a market, then that market will fail. A delicate balance is required for a market to survive, and anything which reduces the liquidity by even a small amount can initiate a vicious circle whereby customer confidence is lost, volume falls, so confidence further falls, and liquidity totally disappears.

A second problem with eliminating dual trading only from liquid contracts is the prevalence of spread trading between illiquid and liquid contracts. A typical spread trade will involve, for example, buying the near liquid expiration month, and selling a later less liquid month. It might even involve selling a less liquid commodity and buying a more liquid commodity. For example, a bond hedger may want to sell federal funds futures (a less liquid contract), and buy treasury bond futures (a more liquid contract), to hedge against a change in the term structure of interest rates.

In order for the spread market to be liquid a trader must be able to do both customer and principal business in both the liquid and illiquid contracts.

A third problem with eliminating dual trading in the liquid contracts is that the volume and liquidity of a particular contract can be quite variable. During periods of unusual weather, a grain futures contract that has had very little volume can show a huge increase in volume. If dual trading is banned from the contract when its volume of trade rises, then when there is a sudden rise in volume, there will be a shortage of brokers and traders to serve customer needs.

2. Eliminate Dual Trading at the Open and the Close of Trading

These are periods of the day with highest volume of trade. It is very easy for order imbalances (for example, a preponderance of customer sells over buys) to appear within a few seconds in this period as brokers attempt to execute "market on open" or "market on close" orders. The market making capital of a broker/trader can become crucial to maintaining price stability in the space of a few seconds. The benefits from switching from brokerage to principal trading can thus appear within a few seconds. This creates benefits from dual trading even at the open and the close of trade.

3. Limit the Size of Customer Orders Executable by a Dual Trader

This would lower the quality of brokerage services to large customers who often need it the most. It would increase price volatility, as large orders have higher market impacts due to execution by less skilled traders. The large traders are the most mobile, and will thus move their orders to foreign markets if they can be executed more effectively there. This will lower the liquidity available to the customers who remain. The customers who remain are likely to be small customers. Hence this limitation on dual trading will harm small customers more than it harms large customers.

4. Limit Dual Trading to the Back Months

I have already noted the problems with eliminating dual trading from liquid contracts. Eliminating dual trading from the front months will make spread trading very difficult, for reasons noted above. However it will also have another subtle, but deleterious effect. It will make it impossible for traders in the back month to hedge their risk in the back month contracts by taking an offsetting position in the front months. For example, a broker/trader who buys a back month contract like the December 1990 bond future (thereby providing liquidity to a customer who wants to sell it) would normally sell the front month to hedge his position. However, if he losses the ability to trade the front month, then he will cease to trade the back month because of the risk involved. Therefore eliminating dual trading from the front months will also cause dual trading to disappear from the back months.

7. Measuring the Benefits of Dual Trading

The previous Sections provide a theoretical overview of the economic role of dual trading and the nature of the benefits customers derive from dual trading. Much of the discussion in the previous Sections can be quantified. In particular, it is possible to measure the contribution made in various futures markets by dual traders. It should be noted that the measurement of the benefits is quite a complex process, and to the best of my knowledge no study exists which has measured the potential losses to the economy of eliminating dual trading.

An empirical analysis of dual trading must begin with an analysis of the extent to which dual trading exists in particular markets, particular contracts, and particular periods. No comprehensive analysis exists of the extent to which an individual member trades for his own account and also trades for customers. The trading records of individual members exist and can be used to reconstruct a record of overall dual trading. This data can be analyzed from two points of view. The first view is "positive", i.e., an attempt to determine what underlying factors have led to the observed historical patterns of dual trading. It would then be determined whether the observed patterns are consistent with the theory of dual trading outlined in the previous Sections. The second view is "normative". This approach will compute the extent to which dual traders have directly and indirectly benefited customers, and the extent to which these benefits would disappear if dual trading is prohibited.

The Determinants of Dual Trading

The theoretical framework developed in this report implies that the following factors will cause dual trading to be important.

1. The extent to which customers desire immediacy of execution. If there are large customer orders which must be "worked" (in the sense that trading it immediately "at market" will give the customer a poor price), but for which the customer bears great risk while the order is unfilled, then there will be a great demand for brokers who are skilled traders.

2. The extent to which customers desire complex spread trades. This is another example where the customer demands brokers with strong timing and bargaining skills.

3. The extent to which there is insufficient customer business or insufficient principal trading business for an individual to earn a living from engaging in only one of these activities.

4. The extent to which there are large swings in the demand for either brokerage or principal trades. Dual trading will be important when there are surprise increases or decreases in customer business which lead to wide and unpredictable variations in the appropriate use of a broker/traders time and effort.

The above factors can be quantified and used in a time series and cross sectional analysis of dual trading, to see if they indeed explain the degree to which dual trading occurs on various futures contracts in various periods.

The Benefits of Dual Trading

The factors emphasized in the previous Sections indicate that dual trading has a direct effect on customers via providing better floor brokerage services, and an indirect effect of increasing market liquidity.

Measuring the direct benefits of dual trading involves the following analysis.

1. Computing the extent to which direct brokerage costs are reduced, for a given level of broker quality, because a dual trader has multiple uses of his time, skills and Exchange seat, and thus can offer to trade at a lower cost.[8]
2. Measuring the extent to which customers receive better executions on complex spreads, and large orders through the use of dual traders.

Measuring the indirect benefits of dual trading on market liquidity involves the following analysis.

1. Computing the extent to which the effective bid ask spread is reduced due to the existence of dual trading.
2. Computing the extent to which the effective bid ask spread is reduced for spread trades.

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[8] "Measuring the Operational Cost of Dual Trading: An Analytical Framework", Kenneth L. Stanley, The Journal of Futures Markets, Vol. 1, No. 3, 329-336, 1981.

3. Computing the extent to which the market can absorb large orders to buy, or large orders to sell with a small market impact (i.e., market depth).

The measurement of effective bid ask spreads, and the measurement of market depth will be accomplished by various methods. All methods will rely upon the idea that trades which have a large market impact and/or are executed against wide bid ask spreads will cause price and expected returns to move in opposite directions. Recall that, for example, a seller will have a large market impact if the price can be expected to rise from the price at which his trade is executed. Various methods will be used to compute the extent to which price and expected returns are negatively correlated, including Roll's measure derived from the autocovariance of period by period returns), and the Grossman-Miller autocorrelation measure, as well as Kalman filtering approaches.[6]

It is important to control for other effects which may impact on actual market liquidity, these effects include variation across contracts in volume traded, average trade size, spot price volatility, time to expiration, the importance of intra-market and inter-market spread trading. Further, it is important to distinguish cause from effect. In particular, the magnitude of the above factors may be either a response to the increase in liquidity caused by the _supply_ of dual traders or instead be factors which contributed to the _demand_ for dual traders.

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[6] These approaches are summarized in : "Economic Costs and Benefits of the Proposed One-Minute Time Bracketing Regulations," Sanford J. Grossman and Merton Miller, Journal of Futures Markets, vol. 6, no. 1, 1986, 141-166. "Liquidity and Market Structure," Sanford J. Grossman and Merton Miller, The Journal of Finance, July 1988, Vol. 43, No. 3, 617-637. "Determinants of Liquidity Costs in Commodity Futures Markets," Review of Futures Markets, Spring 1988. "Inferring the Components of the Bid-Ask Spread: Theory and Empirical Tests," Hans Stoll, Journal of Finance, vol. 44, no. 1, March 1989.

Appendix

Dual Trading In Foreign Markets

In looking at financial markets throughout the world, one finds that dual trading is very prevalent. This is not surprising, given the important benefits that dual trading provides both to brokers and to clients. My preliminary review of world markets indicate that 15 out of 19 countries permit some form of dual trading. Dual trading can take the form of trader/brokers on the Exchange floor as in US futures markets, or the form of banks which act as both principals and agents for customers, or the form of designated specialists, or the form of broker/dealers who can trade on or off the Exchange floor with clients.

The following describes the structure of financial exchanges throughout the world, with regard to brokerage services and dual trading.[7] Unless specifically noted, the Exchanges described are stock exchanges.

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[7] This information was obtained from the following sources. International Society of Securities Administrators Handbook, 1986. European Stock Exchange Handbook, 1973, Noyes Data Corporation, Park Ridge, New Jersey. Major Stock Markets of Europe, Paul Stonham, 1982, St. Martin's Press, New York. The Principal Stock Exchanges of the World, David E. Spray, 1964, International Economic Publishers, Inc., Washington, D.C..

Australia

On the Sydney futures Exchange a local can trade for his own account as well as for other members of the Exchange. He is not permitted to trade ahead of his customer.

On the Australian stock exchange, stockbrokers may trade on their own account, as well as acting for clients. A broker dealer must disclose than he is acting as such. An odd lot specialist is a member broker who exercises a franchise to handle all odd lots. He is able to buy odd lots at a set rate of discount and sell at a set rate of premium, in order to be recompensed for his services.

Options are traded on the Australian options market in much the same manner as ordinary securities. A Registered Trader is required by the exchange to provide a continuous and orderly market by making a market in at least one contract when called upon to do so. He also maintains an appropriate price relationship among the options series in each stock he deals with. A floor trader is a representative of a member firm and executes client orders on behalf of his firm.

Austria

Those holding stock exchange cards include banks and other credit institutions, who may deal directly with each other in purchasing or selling securities. Official brokers may not engage in any stock exchange dealings on their own behalf. The securities quoted on the official list are divided up so that each official broker handles only certain securities. Brokers may also trade off the exchange. Free brokers, who are not officially appointed by the exchange, act as intermediaries between credit institutions, or between clients and credit institutions. They may also trade on their own behalf. Free brokers also deal in securities which may be traded on the exchange floor but which are not officially quoted. All securities may be traded off the exchange.

Belgium

Trading is done exclusively by brokers ("Agents de Change"). These brokers are forbidden to act as a principal. The brokers can receive orders directly from clients or indirectly from corresponding brokers or banks. Corresponding brokers receive orders from clients which they must bring to the brokers for execution. Banks must also go through the brokers to get trades executed, except for orders of over Bfr. 10 million.

Corresponding brokers and banks may act as both agent or principal.

Brazil

Brokerage firms cannot trade for their own account or act as principals. By contrast, investment banks and distribution companies may trade for their own account.

Canada

Member firm brokers trade for their customers and retain a commission as payment. Securities firms who wish to trade listed securities without formally joining the exchange may do so as an authorized non-member. A Registered Trader acts as a dealer in specific stocks assigned to him by the exchange. His function is to act as a market maker in those stocks - to contribute to market liquidity and enhance price continuity. The Registered Trader can execute trades as an agent for a member firm and may also trade his own account, within limitations.

Finland

Most members are banks. Members may trade for their own account as well as for clients. Banks are major investors as well as brokers.

Germany

Clients must place their orders through a bank which is represented on the stock exchange. Banks may trade securities for their own account, take the other side of a customer position, or arrange for another bank to take the other side. They may also place trades through a broker. Official brokers are assigned certain securities by the exchange. Their function is to arrange transactions and set official quotations. The official broker sets a single price for each security which permits him to execute the largest number of orders received for that security. If additional orders are needed to balance existing orders, he calls the quotations to receive them. He may then enter into the trading himself so far as it is necessary to fill existing orders. Otherwise, official brokers are not supposed to deal in their assigned securities for their own account. "Free brokers" execute transactions between banks and may also trade for their own account.

France

Member firms of MATIF, the French financial futures Exchange, are able to execute both proprietary and customer orders.

Securities clients may place orders through a bank or a remisier, an investment advisor. The banks and remisiers in turn transmit the orders to a broker who executes them on the floor or off the exchange. A broker may not trade for his own account or acquire any interest in or any management responsibility for any commercial or industrial enterprise other than his brokerage firm. Banks may also deal directly, off the exchange, including trading on their own account and taking the other side of a customer order.

Hong Kong

All orders must be executed by stock exchange brokers or their employees. Brokers may also trade on their own accounts, as long as these transactions are segregated from those for their clients. Brokers may employ authorized clerks or sales representatives to execute orders on the floor. These employees may not trade for their own accounts.

The Hong Kong Futures Exchange permits dual trading.

India

Any member can act as both a principal or an agent, as long as he provides notification that he is trading for his own account.

Italy

Banks may receive client orders and match them, but all trades executed on the exchange must be done by brokers. The brokers may not trade on their own account nor own any interest or accept any managerial responsibility in any commercial or industrial firm other than their own brokerage firm.

Japan

Regular members of the exchange are companies who both receive orders from clients and trade on their own account. Most regular members also underwrite securities. Special members perform the function of connecting markets by handling orders at the Tokyo or Osaka exchanges which could not be filled on the regional exchanges. Except in situations of unusually high volume, stock exchange members must send orders to the saitoris for execution. These are companies who are responsible for matching orders and fixing the price for those stocks assigned to them by the Exchange. Saitoris cannot trade for their own accounts in the stocks to which they are assigned.

Luxembourg

Stock exchange members are banks or stockbrokerage firms. Stockbrokerage firms may execute trades on their own account as well as for clients. Banks and brokers may trade directly between themselves, without intermediaries. Banks may take the other side of a customer trade.

Mexico

Members are either individual brokers or member firms. Individual brokers may trade for their own account or for a member firm. Brokerage firms may execute orders for clients or trade for their own account.

Netherlands

Banks and brokers receive orders from clients. All orders are transmitted to a hoekman, or specialist. The specialists execute trades in a particular set of securities. They receive a commission form the banks and brokers for performing this function. They may also trade for their own account.

The European Options Exchange is an association set up under Dutch law. Members include banks, brokers, and private traders from North America, Canada, Western Europe and the Far East. Public order members receive orders from the public and pass them to a floor broker for execution. Market makers are traders who are responsible for making a market in those options assigned to them. They act exclusively for their own account.

Singapore

There are three kinds of stock exchange dealer. A stockbroker is a shareholder in a member firm. He may act both for clients and for his own account. A dealer is an employee of a member firm. A remisier is a commissioned agent of a member firm. He may only transact business on behalf of the firm he is employed by.

Trades can also be carried out off the floor and outside of normal hours.

The Singapore International Monetary Exchange is a futures market which permits dual trading by floor broker/traders.

South Africa

Stockbrokers primarily trade for clients, but may also trade on their own account. A "dealer in stocks and shares" primarily trades for his own account, but may also hold himself out to the public. Trading also takes place off the exchange, typically directly between institutional investors, such as banks or insurance companies.

Spain

Orders may be placed through banks or directly with a stockbroker. All orders must be executed by a stockbroker. Stockbrokers may not trade for their own account.

Switzerland

Banks are the only members of the stock exchange. Member banks may trade either on or off the floor. Off the floor trading permits banks to match customer orders against each other. Banks may trade for clients and also trade directly with each other as principals. Formally, most orders are executed by the banks acting as principals.

United Kingdom

The London International Financial Futures Exchange permits dual trading. In particular, Public Order Members are permitted to trade for their own accounts, as well as for customers.

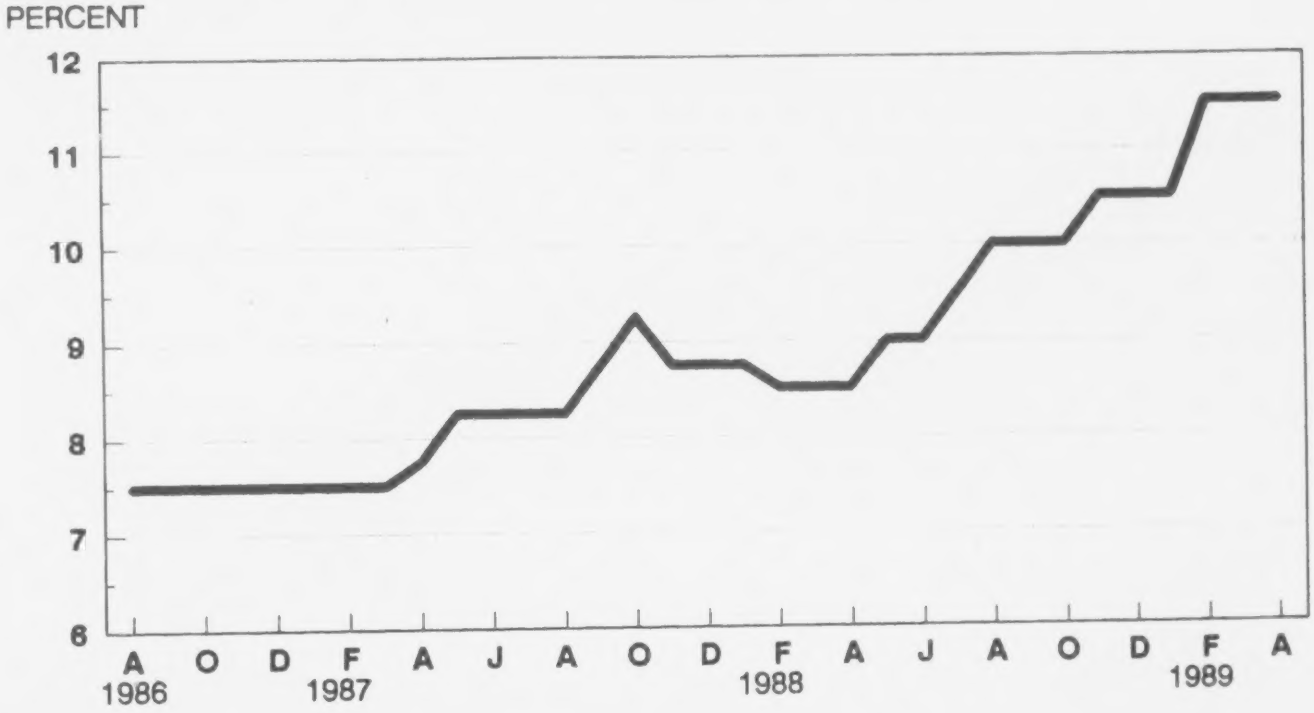
The new securities "market" is based on a system of broker-dealers functioning in a dual capacity, trading as agents for clients as well as principals on their own account. Broker-dealers may also take the other side of a customer order. Certain broker-dealers act as market makers in specific securities. They may deal directly with investing clients. Inter-dealer brokers provide a mechanism through which market makers can trade anonymously with each other. Inter-dealer brokers are not allowed to take positions in stocks. Some market makers are located off the floor in their own trading rooms and trades may be executed by telephone.

United States

The New York Stock Exchange (NYSE) permits the designated specialist to trade as a broker's broker and also to trade for its own account. NYSE broker/dealers can trade for their own account on the NYSE floor as well as for their customers, but

U.S. PRIME RATE

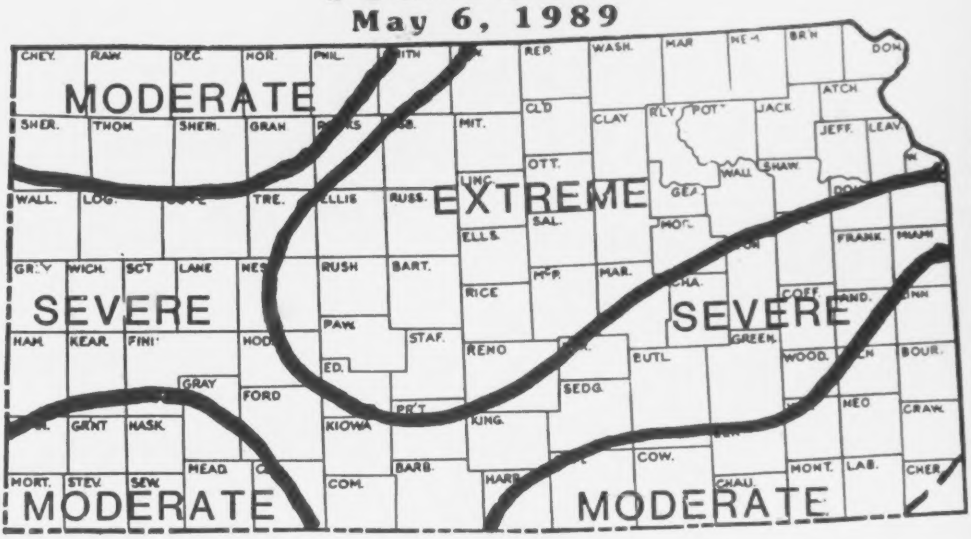
AUGUST 1986 - APRIL 1989



SOURCE: FEDERAL RESERVE BULLETIN, MAY 1989

Kansas

May 6, 1989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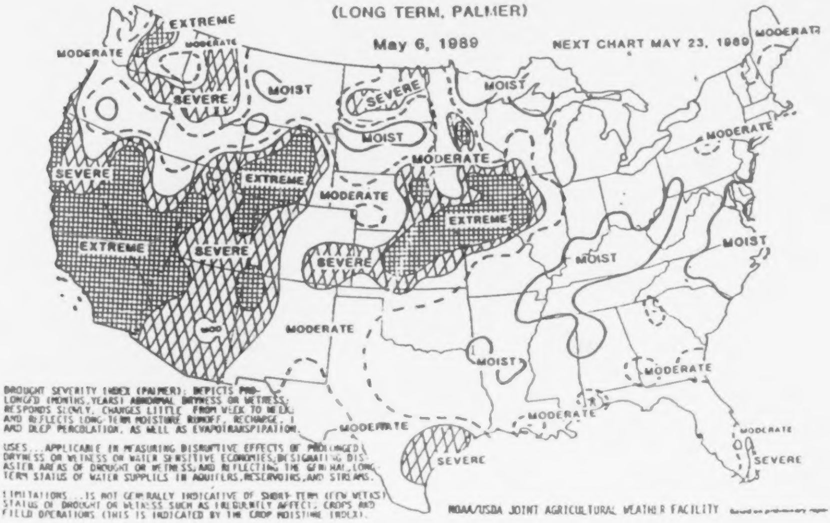
DROUGHT SEVERITY
(LONG TERM, PALMER)
May 6, 1989
NEXT CHART MAY 23, 1989
EXTREME
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NOAA/USDA JOINT AGRICULTURAL WEATHER FACILITY

DROUGHT SEVERITY INDEX (PALMER): DEPICTS PROLONGED (MONTHS, YEARS) ABNORMAL DRYNESS OR WETNESS; RESPONDS SLOWLY, CHANGES LITTLE FROM WEEK TO WEEK; AND REFLECTS LONG-TERM MOISTURE RUNOFF, RECHARGE, AND DEEP PERCOLATION, AS WELL AS EVAPOTRANSPIRATION.

USES... APPLICABLE IN MEASURING DISRUPTIVE EFFECTS OF PROLONGED DRYNESS OR WETNESS ON WATER SENSITIVE ECONOMIES; DESIGNATING DISASTER AREAS OF DROUGHT OR WETNESS; AND REFLECTING THE GENERAL, LONG-TERM STATUS OF WATER SUPPLIES IN AQUIFERS, RESERVOIRS, AND STREAMS.

LIMITATIONS ...IS NOT GENERALLY INDICATIVE OF SHORT-TERM (FEW WEEKS) STATUS OF DROUGHT OR WETNESS SUCH AS FREQUENTLY AFFECT, CROPS AND FIELD OPERATIONS (THIS IS INDICATED BY THE CROP MOISTURE INDEX).

A STATEMENT ON THE CURRENT DROUGHT IN KANSAS[1]

I welcome the opportunity to testify before the U.S. House of Representatives Subcommittee for Wheat, Soybeans and Feedgrains on the current drought.

Summary

The current drought is wide spread in the state of Kansas, and in some counties it is very severe. Current estimates are that financial losses for Kansas farmers and the rural community will be large.

Recently as two years ago, nearly half of the expected revenue on wheat would have been covered by deficiency payments that are tied to program yield and not the currents years production. Because of current price increases, it is expected that none of the current revenue losses on wheat will be covered, unless farmers signup for zero/92 payments. The zero/92 is 92% of $.50, therefore unless yields are well below 10 bushels, this is not an economically viable option and will not cover costs.

An increased number of farmers have signed up for Federal Crop Insurance on their 1989 wheat. Those farmers in the drought areas will be better off financially than their uninsured neighbors. However, insured farmers are not likely to cover the cash flow requirements this year, because the highest crop insurance price election is $3.00 per bushel for wheat losses that are worth over $4.00 per bushel and they have lost the deficiency payment due to the higher than expected price.

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[1] Prepared by G. A. (Art) Barnaby, Jr., Associate Professor, Department of Agricultural Economics, Cooperative Extension Service, Kansas State University, Manhattan, Kansas 66506. Testimony presented to hearing on the 1989 Drought, U.S. House of Representatives, Subcommittee on Wheat, Soybeans, and Feed Grains, Great Bend, Kansas, May 20, 1989.

Farmers continue to be concerned about the method for setting yield guarantees for crop insurance. Also public policies have created economic disincentives for farmers not to purchase crop insurance. A good example is the reduction in emergency feed payments for insured farmers.

Changing current public policies on the procedure used in the Agricultural Stabilization and Conservation Service's (ASCS) commodity programs and Federal Crop Insurance Corporations's (FCIC), Multiple Peril Crop Insurance (MPCI) policies will require additional time for study and implementation. The current financial losses will be covered by farmers equity or crop insurance indemnity payments, unless Congress extends a drought aid program.

Introduction

The current drought has reduced wheat yields by nearly 60% in central Kansas, according to Kansas Agricultural Statistics. The expected production for the state of Kansas is 37 percent below last years crop, with an expected crop of 202.4 million bushels in 1989.[2] Some analyst are projecting an even smaller crop.

Based on Farm Management Association records for South Central Kansas, it cost about $89.05 per acre to produce wheat. Using the estimated yield that is 39% of last year would equal an average yield of 12.9 bushels per acre.[2] If prices were to average $4.10 times 12.9 bushels would yield revenue of $52.89 per acre. If one than subtracts the production cost of $89.05 the net loss per acre would be -$36.16 per acre. The average number of acres was 618 times the loss of -$36.16 per acre for a total average farm loss of $22,347.

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[2] Kansas Agricultural Statistics, Crops, Vol. 89, No. 5, Kansas State Board of Agriculture, U.S. Department of Agriculture, 444 S.E. Quincy, Room 290, Topeka, Kansas 66683, May 11, 1989.

Using the average loss per acre figure for Central Kansas of a -$36.16 times the 1,700,000 planted acres would yield a $61 million dollar direct loss to Central Kansas farms.[3] Those direct losses would then be carried through the local communities and agricultural lenders.

Farmers have used a variety of methods for protecting themselves from production and price risk. Those would include reduced leverage, irrigation, crop share arrangements, diversification, etc. For my testimony I will concentrate on the government commodity program and crop insurance as a method for helping farmers manage risk.

Major Issues

My testimony will address six major issues. Those issues include:

1. The market conditions under which the ASCS commodity program will cover production risk.

2. Why current crop insurance price elections limit the coverage of crop insurance contracts below the value of the loss.

3. The use of the futures markets to set crop insurance price elections.

4. The reduction in other government program benefits for farmers that purchased crop insurance.

5. Proposed policy alternatives to address the price election problems in the crop insurance program.

6. Considerations of the present method for establishing crop insurance yield guarantees.

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[3] Approximately 41 percent of the wheat acres were covered with MPCI crop insurance and would cover a part of this loss.

Government Programs

The government commodity program limits downside price risk and to some extent production risk involved in agriculture, resulting in financial risk reduction for farmers. Multiple Peril Crop Insurance (MPCI) combined with government commodity programs provides additional risk limiting strategies for agricultural producers.

Many farmers consider the deficiency payment in their risk plans. This strategy is satisfactory if crop losses are limited to a small part of the country. A grower that suffers a local drought would not expect market prices to increase, so the deficiency payment would not be affected. Depending on the commodity, the deficiency payment recently ranged from about one-third to nearly one-half of the total revenue. In other words, if the yield losses are local and prices are not effected, then a significant part of the farmers revenue is covered. The reason is that deficiency payments are tied to program yield and not the amount that was actually produced. Several papers have been developed that focus on the substitution of deficiency payments for crop insurance.[4]

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[4] Barnaby, G. A. (Art), Alternatives for Making MPCI Crop Insurance a More Effective Risk Management Tool, Department of Agricultural Economics, Cooperative Extension Service, Kansas State University, 1988.

Williams, Jeffery R. and G. A. Barnaby, Government Programs That Compete With Multiple Peril Crop Insurance, Department of Agricultural Economics, Cooperative Extension Service, Kansas State University, Manhattan, Kansas 66506. Presented at, Risk Management Strategies Utilizing Multiple Peril Crop Insurance: A National In-service Training Workshop for Extension Farm Management Personnel, November 2-4, 1988, Kansas City, Missouri.

Williams, Jeffery R., Jayson K. Harper, and G. Art Barnaby, Mathematical Formulas for Calculating Net Returns from Participation in Government Farm Programs for Major Crops in Kansas: Commodity Program, Crop Insurance, Conservation Reserve, and Disaster Aid, Agricultural Experiment Station, Department of Agricultural Economics, Cooperative Extension Service, Kansas State University, Manhattan, Kansas 66506.

Because of the current dry weather over a large part of the wheat growing region, prices are expected to exceed the target price, therefore growers with below average yields are worse off with high prices. If we assume that the timing of sales is not a problem, so that for every dollar increase received in the market, it results in a dollar decrease in deficiency payments, then one might assume that farmers are just as well off. But the deficiency payments are multiplied by their program yield, which will not vary during the current year's production, while the market price is multiplied times the actual yield produced. Therefore, the grower will gain or lose depending on the following situations:

(a). If his/her actual production yield is less than the farm's government program yield, then the grower actually receives a lower net income as prices rise between the loan rate and target price.

(b). If the grower's actual yield is greater than the farm's government program yield, then the growers net income increases as prices rise.

(c). If the grower is over the $50,000 limit in deficiency payments at low prices, then the growers program yield may be greater than his actual production yield and the grower is better off with higher prices. The amount the program yield may exceed the actual yield and still result in greater financial returns with higher prices, will depend on how much the farmer exceeds the payment limit.

To illustrate the concept, consider the following case farm located in the Central Great Plains. The case farm has a 833.3 acre wheat base and a 10 percent set-aside. The grower plants 750 acres. Consider the following yields on a per acre basis: the expected yield is 40 bushels, a low yield is 20 bushels, and a disaster is a zero yield. This case farm has the following government program for the 1989 crop: 40 bushels program yield, $4.10 target price, $2.57 statutory loan rate, and $2.06 announced loan rate. The grower has a variable cost of $54.14 per planted acre, $10.35 per acre + $0.24 per bushel harvesting and storage cost, and $25 per acre cost for set-aside land.[5]

With a disaster yield (zero yield) and non-participation in the commodity program the grower loses $54.14 per acre plus overhead cost (Figure 1). The revenue is zero because there is no yield to sell, but the grower does save the cost of harvesting.

The grower will have a net return over variable costs of about $22.21 per acre if price is below the $2.06 announced loan and the grower is participating in the government program, as shown in Figure 1. As price increases the deficiency payments from program participation declines, losses start to approach the losses estimated for the grower that is not participating in the program. Losses are still less because there are fewer acres planted.

This graph illustrates the risk problem faced by growers. If the grower has a local drought so that prices do not increase, then the farmer in this example covers the variable cost. But if the drought is wide-spread, causing price increases that approach target price, as in the current situation, then a grower's losses approach that of a grower who is not in the government program.

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[5] Case farm, graphs and analysis prepared by Jeff Williams and Richard Llewelyn, Agricultural Economists, Department of Agricultural Economics, Kansas State University.

Now consider the results for a crop that is one-half of the expected as shown in Figure 2. Once the price reaches $2.06, returns start to decline for the grower in the government program because of declining deficiency payments caused by the actual yield being less than the program yield. Wheat prices would have to reach approximately $4.00 per bushel in this example before the non-program participation strategy would have been better than the program participation strategy.

If the program yield and the actual yield are the same (40 bushels), as depicted in Figure 3, then the market price will have to reach target price for a grower in the government program to receive any additional benefit. With a price of $3.81 or greater, the farmer is better off being out of the government program because the grower received the higher prices on more acres of production.

If a wheat farmer has a below average yield then the best thing that could happen for that farmer is that all others farmers have a bumper crop so that price would fall, thus increasing deficiency payments. Because current price projections are near the target price, one would expect no deficiency payment. Therefore, the commodity program will not cover a very large part if any of the production risk for the current year. In fact, those wheat farmers will be required to repay those advanced deficiency payments.

Federal Crop Insurance

The other major government program that is available for helping farmers manage risk is the Federal Crop Insurance Program. When considering the present Federal Crop Insurance Program many farmers do not participate because of the following reasons:

1. Crop insurance is too complicated.

2. In many cases government has provided supplementary disaster aid when crop losses are wide spread.
3. Crop insurance doesn't cover the expected revenue losses when farmers have a crop failure.
4. Farmers don't like the yield guarantee that is offered.

Let me first emphasize that those farmers with multiple peril crop insurance this year will be much better off then those without. Also, preliminary projections indicate that participation has increased in the Federal Crop Insurance Program by Kansas farmers, from 26 percent to 41 percent.[6]

Public Policy Created Economic Disincentives For the Purchase of Crop Insurance

Congress passed the Agriculture and Consumer Protection Act of 1973 and the Rice Production Act of 1975 and renewed by the Food and Agricultural Act of 1977 that established a disaster payment program for wheat, sorghum, corn, barley, cotton and rice. Later, Congress passed the Federal Crop Insurance Act of 1980 as a replacement for the disaster program and made coverage available for additional crops. United States Congressman de la Garza, (D-Texas), Chairman of the House Committee on Agriculture, through press releases, has made it clear that farmers should depend on crop insurance to cover their crop disaster risks and not count on special legislation that would provide drought aid.[7]

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[6] Source: Gene Gantz, Executive Vice President, American Association of Crop Insurers, 2501 M. Street, N.W., Suite #430, Washington, DC 20037.

[7] de la Garza, E.K., Chairman, Committee on Agriculture, U.S. House of Representatives, De La Garza Concerned About Potential for Drought, Press Release, Room 1301, Longworth House Office Building, Washington, D.C., February 2, 1989.

de la Garza, E.K., Chairman of the Committee on Agriculture, U.S. House of Representatives, De La Garza Urges Participation in Crop Insurance Study, Press Release, Room 1301, Longworth House Office Building, Washington, DC, February 14, 1989.

If one accepts that public policy calls for consistent incentives for farmers to cover their production risk through crop insurance or owner equity, rather than disaster aid, then economic disincentives for the purchase of crop insurance should be eliminated. Those public policy decisions that have created economic disincentives for the purchase of crop insurance include; (1) reduction in emergency feed payments for farmers who collected indemnity payments for crop insurance, (2) 100 percent cap on crop insurance and drought aid, and (3) elimination of the zero/92 option for insured farmers that are faced with substantial yield loss due to the current drought.[8]

Emergency Feed Programs[9]

There are two basic types of emergency feed programs. The first one is the Emergency Feed Assistance Program (EFAP), which provides for the sale of CCC owned grain at 50% of the posted county price to livestock producers whose feed production suffered because of drought or other disasters. The other program is the Emergency Feed Program (EFP), which is a cost share program that helps producers purchase replacement feed which is normally produced on the farm or in quantities larger than would normally be purchased because of a disaster situation. EFAP was authorized by the Agricultural Act of 1949 while

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[8] The cap on payments would have reduced benefits for a very few farmers and is not discussed in this paper. The zero/92 elimination has since been removed from current procedure by U.S.D.A.

A more indepth analysis is included in a paper by G. A. Barnaby, Jr. Public Policy Decisions That Have Created Economic Disincentives For The Purchase of Crop Insurance, Department of Agricultural Economics, Cooperative Extension Service, Kansas State University, Manhattan, Kansas 66506. Presented to the Extension Service - FCIC Crop Insurance Advisory Committee Meeting, Sacramento, California, April 4-6, 1989.

[9] The reduction in the emergency feed program payment to farmers with crop insurance is still current procedure as of May 8, 1989. ASCS has apparently stated that it will change this policy.

EFP was authorized by the Food and Agricultural Act of 1977.[10]

The maximum quantity of feed assistance that producers may receive is ten pounds of grain equivalent per animal unit. The maximum quantity of assistance is reduced by the amount of grain and feed inventory as of the application date.

Any feed held in inventory is included when calculating available feed for meeting the livestock feed requirements. Feed that was purchased is not included, but feed under loan or redeem is included. A livestock owner can not receive assistance in excess of 50 percent of cost of feed purchased or a maximum of $0.05 per pound of feed grain equivalent (FGE).

If the feed loss is covered by FCIC Multiple Peril Crop Insurance then the net indemnity payment is used to "purchase" feed grain equivalents at the rate of $0.10 per pound, or $5.60 per bushel of corn. Because the market value of corn is substantially less than $5.60, the reduction in the emergency feed payment is less than a 1:1 ratio.

An Emergency Feed Program worksheet (1) is included. There are seven sections in the worksheet. They are, I) feed required, II) feed inventory, III) feed produced, IV) net feed required, V) feed lost, VI) reduction for crop insurance, and VII) benefit. The worksheet is demonstrated using the following example.

In section I, the number of animals, the appropriate animal units (AU), and number of days the animals need feed during the emergency is entered. The total amount of AU's required is then estimated (line 4). Line 5 through 8 contain a section for entering young animals. The total AU's, for mature animals and young animals is entered on line 9. The pounds of feed per animal unit required is entered on line 10, with 10 pounds per animal unit as the maximum. Then calculate the total pounds of feed required by multiplying line 9 by line 10.

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[10] Lipton, K. and S. Pollack, The Disaster Assistance Act of 1988: A Description of the Provisions, Economic Research Service, USDA, 1301 New York Avenue, N.W., Washington, D.C., September 1988.

The feed in inventory at the time of application is then estimated. In this example, the producer has 100 bushels of corn and assuming it weighs 56 pounds per bushel the corn inventory is 5,600 pounds. Alfalfa hay is estimated next. In this example there is 20 tons in inventory. Total feed grain equivalent (FGE) pounds is estimated using a factor of .64 to arrive at a total of 25,600 pounds of alfalfa hay FGE. The factor provided by ASCS is used to adjust forages to a feed grain equivalent. Any other feed held in inventory also needs to be accounted for in pounds of FGE. In this example, the total is 31,000 pounds of FGE (Worksheet 1, Line 17).

Section III, is used to estimate the amount of feed produced on the farm.[11] In this example the farmer has 50 acres of corn. Assuming a current year's production of 30 bushels per acre, would equal 84,000 pounds of FGE. The example also includes 28 acres of alfalfa hay, with a 1 ton per acre yield. Using the appropriate FGE factor of .64 there is 25,600 pounds FGE of alfalfa hay available. In section IV, the net feed required is estimated, and is calculated using the total pounds of feed required (line 11) minus total pounds of FGE in inventory (line 17) minus total pounds of current production of FGE (line 22). In this example, there is a net of 156,200 pounds of FGE.

Section V is used to estimate the amount of feed lost. Farmers must have feed losses in excess of 40% to be eligible for any feed assistance. In this example, there is 50 acres of corn, with an average yield of 115 bushels per acre. The average yield of 115 bushels per acre less the current production is 30 bushels per acre, times 56 pounds per bushel, resulting in 238,000 pounds of feed lost (line 23). Calculation for alfalfa is similar and results in 102,400 pounds of FGE lost.

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[11] If this worksheet is completed after harvest, the production would be included in the feed inventory section.

Section VI is for estimating the reduction in FGE's resulting from the purchase of crop insurance. The APH yield for crop insurance is entered on line 29 and the selected coverage level is entered on line 30. The APH yield is multiplied by the coverage level to determine the yield guarantee (line 31). The current production (line 32) is subtracted from the guarantee (line 31) to determine the bushels lost (line 33). The lost production (line 33) is multiplied by the price election (line 34) to estimate the indemnity payment (line 35). The insurance premium (line 36) is subtracted from the indemnity payment (line 35) to determine the net indemnity payment (line 37). Each 10 cents of net indemnity payment received is equivalent to one FGE. Therefore, the net indemnity payment is divided by 10 cents to determine the number of FGE's per acre (line 38). The FGE's are multiplied by the number of acres to yield the total FGE's covered by crop insurance (line 10).

Section VII is for estimating the total benefits, based on the payment rate (line 42) times net feed required (line 43).

Outcomes for Emergency Feed Programs

The example provided in worksheet 1 demonstrates how emergency feed payments are reduced as a result of purchasing crop insurance. The total payment reduction is $2,155.25. For each dollar in net indemnity payments received, it would have reduced the case farm emergency feed payment by approximately 50 cents.

Because the emergency feed program is an on going program, farmers could cover part of the crop production risk for corn, milo and other feed grains using this program and saving the crop insurance premiums. Farmers that adapt this strategy do take the chance that a disaster would not be declared and therefore, the emergency feed program would not be implemented. Farmers must also retain low feed inventories in order to make this strategy work.

The Emergency Feed Program is a good example of how other government programs reduce the economic advantage for the purchase of crop insurance. Much of the university research has focused on crop insurance as a risk tool and the rate structure relative to the risk exposure.[12] Had those studies included an emergency feed program strategy that reduced emergency feed payments for insured farmers, then the results would likely be different.

While the effects on crop insurance participation at this point may be more psychological than economic, continued public policies that allows other government program benefits to be reduced for farmers that purchased crop insurance, will cause farmers to reduce their participation over time. Many farmers that signup for crop insurance probably never anticipated that other government benefits might be denied. If Congress wants to expand crop insurance participation, then it will be necessary for Congress to eliminate public policies that allow other government farm programs available to uninsured farmers from being reduced or denied to insured farmers.

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[12] The following papers are examples of research that does not include any of the risk substitution caused by the public policies discussed in this paper.

Harper, Jayson K., Jeffery R. Williams, and G. A. Barnaby, Selecting Risk Efficient Crop Insurance Alternatives for Northeast Kansas Corn/Soybean Farms. Kansas Agricultural Experiment Station, Cooperative Extension Service, Department of Agricultural Economics, Kansas State University, Manhattan, Kansas 66506. Submitted for consideration as a selected paper for the WAEA meetings in Coeur d'Alene, Idaho, July 9-12, 1989.

Harper, Jason K., Jeffery R. Williams, and G. A. Barnaby, The Effect of Drought Risk on the Selection of Government Program Strategies for Corn in Northeastern Kansas, Kansas Agricultural Experiment Station, Cooperative Extension Service, Department of Agricultural Economics, Kansas State University, Manhattan, Kansas 66506. Submitted to the North Central Journal of Agricultural Economics, 1989.

Pfleuger, Burton W. and Peter J. Barry, "Crop Insurance and Credit: A Farm Level Simulation Analysis", Agricultural Finance Review, 46(1986): 1-14.

Problems With Crop Insurance Price Elections For Program Crops

Crop insurance contracts will not cover necessarily the losses of Kansas farmers, because of price increases for wheat. For example, this year insured wheat farmers in Kansas will be paid a maximum of $3 per bushel for lost production. However, the value of that lost bushel at harvest time is expected to be $4 or more.[13] At a price of $4, farmers will lose most of their deficiency payment, but if they have an average crop and receive the higher price they will generate the same total revenue. Without an average crop those insured wheat farmers will receive an indemnity payment based on the $3 price election and receive a small or no deficiency payment, so MPCI fails to cover the revenue losses the farmer experienced. The price election could have worked the other way as it did a few years ago with the raisin harvest. MPCI price elections were much higher than the market price for raisins so the grower had every economic incentive to "lose" the crop.

The crop insurance price election on ASCS program crops often does not equal the expected value of the crop, less the deductible. That is growers that purchase an MPCI policy with 75 percent coverage, can not cover 75 percent of their expected revenue (including government commodity payments) for a program crop.

Growers with a 40 bushel program yield for wheat and target price of

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[13] Market prices will depend on the supply of wheat and that is currently being determined by future weather effects as of May 15, 1989.

$4.10 would expect their revenue per acre to be $164.00. Growers that participate in the ASCS wheat program and purchase crop insurance at the 75 percent level would expect to draw a minimum of $123.00 in cash, should they have a zero yield. However, because of current policy rules in the ASCS and FCIC programs growers don't necessarily end up at that level. Price elections for the commodity that determine indemnity payment rates on lost production, must be estimated 7-9 months in advance of harvest.

Based on 1989 wheat price estimated by FCIC, the top price election was $3.00. Growers that purchased a 75 percent contract with a $3.00 price election and suffered a total crop loss while at the same time prices increased to the target level then they would only receive 53 percent of their expected revenue (Figure 4). Growers that purchased a 65 percent contract would have covered only 46 percent of their expected gross revenue (Figure 5). In this case, growers' revenues consist of a $90 indemnity payment less a premium of $3.51 for a net of $86.49 per acre.[14] On the other hand if prices had stayed at the $3.00 level as forecasted by FCIC when they estimated the price elections for wheat then growers would have received $44 in deficiency payments plus $86.49 indemnity payment for a total of $130.49 or 80 percent of expected revenue (Figure 4).

It is also possible for the price elections to end up above the market price. This would have been the case if market price had been equal to the statutory loan rate of $2.57 versus the $3.00 price election (Figure 6). Farmers would then receive indemnity payments per covered bushel that are $0.43 above the market price and covered 90 percent of the expected revenue

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[14] The insurance rate used is for wheat in McPherson County, Kansas. The price election is for the 1989 crop.

(Figure 4). With price elections above market prices, and a below average crop, there is an economic incentive to lose production.

Market Price Election

One proposed method is to use the futures markets to set price elections. Currently the top price election for soybeans is based on the last 5 trading days of March for the Chicago Board of Trade (CBT) November futures contract. Those five closing prices are averaged and multiplied by 85 percent to yield the market price election for 1989 soybeans.

If a similar procedure had been applied to the 1989 winter wheat contract, the resulting price election would have nearly equaled the current top price election for 1989 wheat. Using the proposed procedure of averaging closing prices during the month of August 1988 for July 1989 wheat on the CBT, and multiplying by 85 percent would have generated a price election of $3.01 (Table 1). Given that the top price election for the 1989 MPCI wheat contract was $3.00, the use of the futures market to set price elections would not have corrected the price election problem that was demonstrated in Figure 4.

Depending on price, growers may cover from 53 percent to 102 percent of their expected revenue by purchasing a crop insurance with 75 percent coverage and participating in government ASCS commodity programs. As price falls, more of the grower's expected revenues are covered with ASCS payments. But if the disaster is wide spread, then prices tend to rise and the resulting coverage from crop insurance and commodity programs are at its lowest just when farmers need the protection (Figure 4).

Two Possible Alternatives For Addressing the Price Election Issue

I. Retain Expected Deficiency Payment on Indemnity Bushels.

An alternative approach for the current method of price elections would be to utilize the estimated deficiency payment and crop insurance combining both into a risk program for farmers. For example, on 1989 wheat the estimated deficiency payment was $0.50 and the top price election on crop insurance was $3.00. Using this approach, growers could purchase crop insurance at the estimated market price level, in this case $3.00 and at the same time retain the estimated deficiency payments on the bushels that indemnity payments were paid on. Under this plan the grower would not be guaranteed the estimated deficiency payment on the deductible bushels which would be the first 10 bushels in this example. But the grower would receive the $0.50 estimated deficiency payment on any part of the 30 bushels that are guaranteed and are not actually produced.

Logic behind this concept is that, if farmers produce any of those 30 bushels that are guaranteed they would receive the higher market price for those bushels and so the deficiency payment is not necessary. On the other hand if growers do not produce the yield then the higher price does them no good.[15]

Using an example with a zero yield, growers would draw $0.50 deficiency payment on the 30 bushels that are guaranteed. They would also receive $86.49 net indemnity payments from the crop insurance. This would yield growers 62 percent of their expected gross sales using this particular example versus 53 percent without deficiency payments (Figure 7).

Had both ASCS and FCIC used the same price forecast of $3.00 then the combination of crop insurance and the estimated deficiency payment paid on indemnity bushels, would have allowed farmers too cover nearly 75 percent of their expected revenue (Figure 8). If ASCS had used a $3.00 price forecast then the estimated deficiency payment would have been $1.10 versus the current $0.50.

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[15] It is the same logic as guaranteeing the estimated deficiency payment for the zero/92 program where farmers have no production to take advantage of higher prices.

For this to be an effective approach, then both ASCS and FCIC would need to use the same price forecast.

This approach is not the same as payment of deficiency payments to all farmers as was originally considered in the recent Disaster Assistance Act of 1988, for three reasons.

1. Estimated deficiency payments would be guaranteed only to holders of FCIC crop insurance contracts. The difference between the target price less the estimated deficiency payment would be covered by the top price election in the MPCI contract. The balance of any deficiency payments would be subject to market prices, as it is under current policy.
2. The estimated deficiency payments under this plan are not guaranteed on the deductible.
3. Farmers that do not participate in the crop insurance program would not have their estimated deficiency payments guaranteed, but would be subject to market prices as is currently the policy.

Consequences

At the start of the year, farmers expectations were to draw a deficiency payment of $1.10 plus the expected market price of $3.00.[16] Because of the widespread drought and the resulting price increases obviously this will not be the case. This approach would require FCIC and ASCS to use the same estimates for calculating the expected deficiency payment plus the top price selection for crop insurance prior to the planting season.

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[16] At planting time, many analyst expected a price of $3.00 because of additional acreage planted. ASCS announced the program after planting and resulted in a higher price estimate of $3.60.

2. The estimated deficiency payment is budgeted in the current appropriations and therefore would fit into current federal government projections. At the same time the deficiency payment under this plan would not be due on the deductible portion and therefore would be retained by the Federal Treasurery subject to market prices. Farmers would gain from the stand point that they are now able to protect nearly 75 percent of their expected revenue, that was their real objective versus 53 percent of their projected revenue using strictly crop insurance, under present rules (Figures 4 and 8). This analysis assumes that Congress does not provide any disaster relief payments.[17]

3. This approach would reduce potential government savings. The budget already includes the projected outlays based on estimated deficiency payments, but if prices were to increase, it would save the government money that would have been spent on deficiency payments.

4. If market prices at harvest time end up lower than the price estimate by ASCS and FCIC, then FCIC still has a "moral hazard" on price elections.

II. Dollar Liability Crop Insurance

Another alternative for addressing the price election issue is the sale of a dollar liability policy. Using some of the sales principles that the private industry utilizes with Private Hail Insurance (PHI), the proposed dollar liability MPCI policy would be sold using the following outline:

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[17] Instead of 75 percent crop insurance contract used in this example farmers that purchased 65 percent contract, plus the estimated deficiency payments on indemnity bushels would have covered approximately 65 percent of their expected revenue.

(1). Sell Farmers any dollar amount of liability they wish to purchase;[18]

(2). Allow the farmer to select a bushel deductible;

(3). Prove individual farm yields with records.

Outcomes Based on Dollar Liability Crop Insurance

1. A dollar liability would simplify the program because growers would simply select the desired coverage and deductible, similar to other lines of insurance.

2. There is no need for forecasted price elections.[19] Losses would be paid based on the current value of the crop that was lost, up to the limits of liability selected by the farmer at signup time. This would cover the current wheat crop losses at market value not a price of $3 that was forecasted nearly a year in advance. This approach also would prevent FCIC from paying losses at a value greater than market, as was the case for raisins where market prices were well below the price elections, thus creating an economic incentive to lose the production.

3. This approach also eliminates the deficiency payment considerations. With high prices, insured growers are either paid for crop losses based on harvest time market prices or they have production to sell at higher prices. If prices are low, then growers receive a deficiency payment that is not tied to current production to offset low prices. Those insured farmers that have

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[18] For actuarial reasons, FCIC may need to place minimum and maximum levels on the amount of liability purchased by growers.

[19] A price forecast would be needed internally by FCIC for the purpose of setting the dollar liability limits.

no production would receive indemnity payments based on the current lower market prices. Therefore, there is no economic incentive to lose the crop and collect indemnity payments based on higher price elections than current market prices.

4. This approach would cover the value of loss on non-program crops, e.g. soybeans, where deficiency payments are not a consideration.

Current Law and the Dollar Liability Approach

Farmers would purchase a dollar liability, MPCI policy with a "bushel" deductible for actuarial reasons. For example, a 40 bushel guarantee would have a 10 (14,20) bushel deductible, i.e. the same as the current 75 percent (65%, 50%) coverage. Losses beyond the 10 bushels would be covered at current market prices, up to the limits of the dollar liability purchased.

In our example, using a 10 bushel deductible resulting indemnity payments would be paid after the yield falls below 30 bushels (Table 2). Losses would be paid based on current market prices and with low prices farmers would not collect all of their purchased liability. With high prices they would exhaust their liability limit before reaching zero yield.

This approach of a bushel deductible combined with a dollar liability would eliminate the "moral hazard" on price elections. With a 10 bushel deductible, indemnities would be paid on production lost below the guarantee of 30 bushels, but at the current market price, rather than on forecasted price elections.

Farmers' price risk would have to be covered by other methods that are available to them. Farmers that participate in the ASCS program would receive deficiency payments if prices decline. Farmers that forward contract would be in a better position to cover those contracts with a dollar liability program.

If losses were paid at the market price, then farmers would be able to purchase grain to cover their forward contracts. Under the current FCIC program for wheat, farmers will receive $3.00 for lost wheat production, but would need to purchase wheat at a current market price of $4.00 or more to cover the forward contract. In this case farmers lose twice, once on production and once on price.

Revenue Insurance

This approach is not revenue insurance because if market price declines but farmers have normal wheat yields of 40 bushels combined with a low price of $2.00 then their total revenue is $80. Because those farmers had normal yields, there is no indemnity payment due, yet those farmers had very low total revenue. With program crops farmers would receive deficiency payments that would offset price declines.

This approach is only insuring farmers' yields and if price declines the value of any lost bushels would also decline. FCIC would then pay losses based on a current lower market value, i.e. FCIC would only pay the value of the loss. Under the current system in many cases it is possible for FCIC to pay losses based on price elections that are above the market.

Rating Considerations For This New Product

If, based on an internal price forecast, FCIC would set a minimum and maximum amount of liability that could be sold on a crop, then FCIC would have the same risk exposure they currently have, if their price forecast was always correct.

For example, if FCIC forecasted a price for wheat of $3.00 and at harvest time the price was $3.00 the outcome would be the same as it is in the current system (Table 3). The indemnities would be paid at a current market value of

$3, which is the same as the price forecast at signup time.

Think of the insurance company as an elevator holding 30 "bushels" of wheat that would be paid out to the farmer if his/her yields fall below the guarantee. As in the case of an elevator holding grain in storage, everything is fine as long as price does not move against them. An elevator holding grain would go into the futures market and protect themselves against adverse price movements.

In this case assume that the insurance company would use call options to protect themselves from price increases on the 30 bushels they have insured with the farmer. If the price increases to $4.00 then the insurance company is covering the value of the farmers loss at the current market value of $4.00. If the insurance company has based their indemnity payment on a $3 price forecast, then they would "lose" $1.00 for each bushel that losses are paid on. Because the farmer must purchase a fixed dollar liability policy, the insurance company would limit total exposure to that amount. In column 2 of Table 3, no additional indemnities would be paid once yield reaches 7 bushels or less because of the dollar liability limit.

Secondly, the insurance company limits their risk exposure by using call options or a hedge in the futures market. If price increases to $4 and the insurance company has covered the 30 bushels with call options, then they gain $1.00 in the futures market that offsets additional dollars paid out.

If price were to decline to $2 as shown in Table 3, column 3, then the insurance company pays out $1.00 less per bushel than they would have in the present system with price elections.

This approach would "add" price risk to the crop insurance contract. If prices go down the insurance company gains because of the value of paid losses are declining. But if price were to increase then value of losses paid would increase and the insurance company would lose unless they had passed the price risk onto the futures market.

I would argue there is price risk in the current program. If prices fall, insurance companies have a "moral hazard" on price selections that are above market. Recently, I presented the example of a $3.00 price election and $2.00 market price to a group of about 150 farmers. I then asked, "how close are you going to set the combine?" While getting a good laugh, I think the point was well made. Price risk has always been in the crop insurance program, and I am only suggesting that it be managed rather than ignored.

Is This Practical?

With the requirements for premiums on options, it may not be practical for a government agency like FCIC to use options (or futures) to protect against price risk. Margin calls can not wait on someone to make decisions, cut checks, and meet work schedules.

Managing this fund would require employees with futures and options trading skills. This is exactly the type of price risk that major grain companies manage everyday.

Profit Potential for a Private Company

An alternative, may be for FCIC to underwrite the yield risk while the private companies handle the price risk. A private insurance company using the futures market is probably something they have never been involved with. But conceptually it is not very different from what is currently done by an insurance company. An insurance company will insure something of value and then decide how much risk they want to retain versus sell off to a reinsurance company. The Chicago Board of Trade and other commodity exchanges are simply the "reinsurance" companies.

Profits

The insurance company has the opportunity to make additional profit if price declines from the forecast. In Table 3, column 3, the insurance company is now paying losses at a lower rate because of price declines. In addition the liability for the insurance company has declined to $60 even though the farmer purchased $90. Remember this is not revenue insurance, farmers will have to cover price declines by participation in the ASCS commodity programs or with their own marketing plan.

If prices increase then the calls and future hedges would protect the insurance company from losses. But the purchase of those calls would also cost the insurance company, as it does when the insurance company sells off a part of its risk to a reinsurance company.

However, would insurance companies use the futures market to protect itself on the full amount of bushels insured? Using the example in Table 3, column two, call options purchased for bushels below a yield of 7 bushels is not necessary because the dollar liability is exhausted and no additional indemnity payments are made beyond that point. That is, the insurance company would need to cover price on 23 bushels of potential losses not the full 30 bushels of losses.

In addition, insurance indemnities are not likely to be paid on all of the "bushels" they have insured. So they may wish to retain some of the risk and pass on to the futures market price risk only on bushels they are likely to pay indemnities on. They then reduce their hedging costs.

Also, by offering the farmer a policy based on a dollar amount and paying losses at the current market value, if it should result in better acceptance of MPCI by farmers, then increased profits would be generated with increased sales of MPCI policies.

Finally profits would be improved by better loss control. Because indemnities would be paid on the current value of the loss rather than the pre-signup forecasted price, FCIC and the insurance company would never be in the position of paying more for a loss than it is worth in the market. This would reduce the "moral hazard" on price elections that insurance companies face when price elections are higher than market price. The removal of the "moral hazard" should improve product integrity.

Yield Guarantee

In addition to price elections, many farmers also believe the yield guarantee offered is two low. Farmers tend to over estimate their yields because they forget the bad years and remember the good years. Many Kentucky farmers who were surveyed in 1987 did not include the worst crop production year that they had as even a possibility, and the worst year occurred in 1983.[20]

FCIC also changed their method for computing yield guarantees. A few years ago they used an "olympic" average where they eliminated the low yield and the high yield and averaged the remaining years of yield data. FCIC currently uses a 10 year simple average, which was done to "simplify" the program. However, the simple average may have reduced farmers' yield guarantees below their long run average yields.

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[20] Source: Based on research by Jerry Skees, unpublished manuscript, reported to Extension Advisory Committee on Crop Insurance, Department of Agricultural Economics, University of Kentucky, Lexington, Kentucky.

The use of simple average is a reasonable assumption for yield guarantees if yield distributions are symmetrical and bell-shaped (Figure 9). But if yields are negatively skewed as drawn in Figure 10, then there is a chance of drawing a very low yield in the long downside tail of the distribution but very little chance of drawing an offsetting value in the upside tail.

FCIC currently uses a simple average to base yield guarantees on, and if yield distributions are negatively skewed then there is a good chance that the simple average will underestimate the true mean. By using a 5 year average as has been proposed rather than a 10 year average, a single value in the downside tail will have an even greater influence on the yield guarantee.

If yields are negatively skewed, then farmers are better off with the "olympic" average than a simple average. It also will prevent a farmer's yield guarantee from being reduced because of a single claim.

Conceptional Reasons for a Negative Skewed Yield

Zero yields are possible for most crops in the U.S., either caused by hail, drought or other weather problems. Upside yields are constrained by the soil, genetic make up of the plant, technology, and management level. While dryland corn farmers in northeast Kansas may have zero yields there is almost no chance that those farmers would raise a 200 bushel yield.

Evidence of Negative Skewed Yields

Gallagher suggest that yields may be negatively skewed based on national average corn yields. Gallagher argues that corn yields are skewed because the corn plant can not exceed the biological potential of the plant. Furthermore, failure to recognize this skewed yield distribution causes one to underestimate the most likely yield.[21]

A similar result was found using individual farm yield data for Northeast Kansas corn farms.[22] Yields for 52 Northeast Kansas corn farms in the Kansas Farm Management Association are presented in Tables 4 and 5. The average yield, lowest yield, highest yield, and a measure for skewness on each farm is presented for a 10 year period (Table 4) and a 15 year period (Table 5). This actual farm corn yield data would also suggest that yields maybe negatively skewed.

In Figures 11 and 12, the skewed value measurement is plotted by average yield from the lowest to the highest average yield. Average corn yield are labeled on the bottom axis with the corresponding skewed value plotted. For this set of yields there appears to be some relationship between average yield and skewness. Farmers with the highest average yield would appear to be more likely to have yields that are more negatively skewed than those farms with lower average yields.

If farmers with high average yields are less likely to use the program yield or the current T yield as a "floor", then "olympic" averaging is very important for the top producer. If yield distributions are more negatively skewed with higher average yields as suggested by Figure 11, then "olympic" average is more important for the top producing farmer.

Closing Thoughts

The current drought is wide spread in Kansas and will cause financial losses for many farmers. While my testimony has focused on addressing problems with the ASCS commodity program and the crop insurance program, these are "long run" public policy considerations.

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[21] Gallagher, Paul, "U.S. Corn Yield Capacity and Probability: Estimation and Forecasting with Nonsymmetric Disturbances", North Central Journal of Agricultural Economics, Vol. 8, No. 1, January 1986, pp. 109-122.

[22] Similar work is being done with wheat yields but has not been completed.

The current drought caused losses will either be covered with farmers' equity or government disaster payments. Those farmers that purchased crop insurance will limit the loss of their owner equity, but because of wheat price increase even they will not cover a large part of their cash flow requirements.

(Attachments follow:)

Worksheet 1. Emergency Feed Program

I. Feed Requirements

		With Insurance	Without Insurance
	Mature Animals		
1.	Number of Animals	150	150
2.	Number of A.U. per animal	1.0	1.0
3.	Number of days for feed emergency[1]	180	180
4.	Sub Total A.U. for mature animals (Line 1 x Line 2 * Line 3)	27,000	27,000
	Young Animals (6 mo. - 1 year)		
5.	Number of animals (6 mo. - 1 year)	30	30
6.	Number of A.U. per animal	.5	.5
7.	Number of days for feed emergency	180	180
8.	Sub Total A.U. for young animals (Line 5 * Line 6 * Line 7)	2,700	2,700
9.	Total A.U. required (Line 4 + Line 8)	29,700	29,700
10.	Pounds of feed per A.U.[2]	10	10
11.	Total pounds of feed (Line 9 * Line 10)	297,000	297,000

II. Feed Inventory

Crop		Units	Lbs./Unit	Factor	Lbs. FGE	
12.	Corn	100 bu.	x 56	x 1	= 5,600	5,600
13.	Alfalfa	20 Tons	x 2000	x 0.64	= 25,600	25,600
14.			x	x	=	
15.			x	x	=	
16.			x	x	=	
17.	Total Lbs. of Inventory Feed (Sum Lines 12 - 16)				31,200	31,200

III. Feed Produced.

Crop		AC	Yield/AC	Lbs./Unit	Factor[3]	Lbs. FGE	
18.	Corn	50	x 30 bu.	x 56	x 1.0	= 84,000	84,000
19.	Alfalfa	20	x 1 ton	x 2000	x 0.64	= 25,600	25,600
20.			x	x	x	=	
21.			x	x	x	=	
22.	Total Lbs. of Production (Sum Lines 18 - 21)					109,600	109,600

IV. Net Feed Allowance (Line 11 - Line 17 - Line 22) 156,200 156,200

OR:

V. Feed Lost[4]

Crop		AC	(Ave. Yd - Yd)[5]	Lbs/Unit	Factor	Lbs. FGE	
23.	Corn	50	x (115 - 30)	x 56	x 1.0	=238,000	238,000
24.	Alfalfa	20	x (5 - 1)	x 2000	x 0.64	=102,400	102,400
25.			x	x	x	=	
26.			x	x	x	=	
27.	Total Lbs. of Feed Lost (Sum Lines 23 - 26)					340,400	340,400
28.	Lesser of Net Feed Required or Feed Lost (Lesser of Line IV. or Line 27)					=156,200	156,200

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[1] Feed days are set by county committee.

[2] 10 lbs. per animal unit is the maximum allowance, even if you are feeding more than 10 lbs. The animal units are adjusted for animal species and age.

[3] Forages are adjusted to feed grain equivalent. Factor list is available from ASCS.

[4] Must have 40% loss to be eligible for assistance.

[5] Feed production loss are based on losses in excess of 40%. If you have already collected drought aid on the lost crop production, then you may not count the loss on the feed worksheet.

WORKSHEET 1, CONTINUED

VI. Crop Insurance Adjustment		
29. Average T Yield or APH for Insurance	115	0
30. X Coverage Level (50%, 65%, 75%)	65 %	0
31. = Bushels/Acre Yield Guarantee	74.75	0
32. - Less Current Year's Crop	30 bu.	0
33. = Bushel Loss/Acre	44.75	0
34. X Price Election	2.00	0
35. = Indemnity Payment/Acre	$ 89.50	0
36. Less Premium	$ 3.29	0
37. Net Indemnity Payment/Acre	$ 86.21	0
38. FGE Covered With Crop Insurance @ 10 ¢/lb.	862.1	0
39. X Acres	50	0
40. = Total FGE Covered With Crop Insurance	43,105	0
41. Net FGE (Line 28 - Line 40)	113,095	156,200
VII. Benefits		
42. 50% of Cost Share or Maximum of $0.05 per FGE	.05	.05
43. Net Feed Required (Line 41)	113,095	156,200
44. Government Payment (Line 42 x Line 43)[6]	$ 5,654.75	$ 7,810

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[6] Results checked against DAP, Release 1.2, computer software by Center for Farm Financial Management, Minnesota Extension Service, University of Minnesota.

TABLE 1. CHICAGO BOARD OF TRADE CLOSING PRICES FOR JULY 1989 WHEAT

Date	Closing CBT Prices	Date	Closing CBT Prices
August 1, 1988	$3.535	August 17, 1988	$3.53
August 2, 1988	3.52	August 18, 1988	3.5525
August 3, 1988	3.53	August 19, 1988	3.53
August 4, 1988	3.5425	August 22, 1988	3.445
August 5, 1988	3.53	August 23, 1988	3.465
August 8, 1988	3.50	August 24, 1988	3.535
August 9, 1988	3.505	August 25, 1988	3.575
August 10, 1988	3.53	August 26, 1988	3.53
August 11, 1988	3.53	August 29, 1988	3.52
August 12, 1988	3.52	August 30, 1988	3.63
August 15, 1988	3.61	August 31, 1988	3.6425
August 16, 1988	3.565		

Sum of the Closing prices = $81.3725
Divided by 23 day = $ 3.5379
Times (Basis Factor) 85%
Equals Market Price Election $ 3.01

TABLE 2. COMPARISON OF CURRENT 1988 MPCI POLICY ON WHEAT VERSUS MPCI POLICIES WITH A BUSHEL DEDUCTIBLE DOLLAR LIABILITY

	Current With a $4 Harvest Price	Alternative With A $4 Harvest Price	Alternative With a $2 Harvest Price
Average Yield	40	40	40
x % Coverage	75%	-	-
= Bushel Guarantee	30	-	-
x Price Election	$ 3		
= Liability	$90	$90	$90
$ Deductible	-	10 bu.	10 bu.
Deficiency Payment	$ 4	$ 4	$81.60
Gross Indemnity[1]			
Yield			
30	$ -	-	-
29	$ 3	$ 4	2
28	6	8	4
27	9	12	6
26	12	16	8
25	15	20	10
24	18	24	12
23	21	28	14
22	24	32	16
21	27	36	18
20	30	40	20
19	33	44	22
18	36	48	24
17	39	52	26
16	42	56	28
15	45	60	30
14	48	64	32
13	51	68	34
12	54	72	36
11	57	76	38
10	60	80	40
9	63	84	42
8	66	88	44
7	69	90[2]	46
6	72	90	48
5	75	90	50
4	78	90	52
3	81	90	54
2	84	90	56
1	87	90	58
0	90	90	60

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[1] Premium would be rate times liability. Rate would change on the alternative based on size of the dollar deductible chosen by the farmer.

[2] The indemnity would not increase for the additional lost bushel because the farmer has reached the maximum liability that he/she chose.

TABLE 3. MPCI POLICIES WITH A BUSHEL DEDUCTIBLE, DOLLAR LIABILITY, THREE PRICE ASSUMPTIONS, AND $3.00 PRICE FORECAST

	Alternative With A $3 Harvest Price	Alternative With A $4 Harvest Price	Alternative With A $2 Harvest Price
Market Forecast and Signup	3	3	3
Harvest Time Price	3	4	2
Average Yield	40	40	40
= Liability	$90	$90	$90
Deductible in Bushels	10 bu.	10 bu.	10 bu.
Deficiency Payment	$ 4	$ 4	$81.60

Market Price	$3.00	$4.00			$2.00	
Yield	Indemnity	Indemnity	Loss/Gain On Price	Futures Account	Indemnity	Loss/Gain On Price
30	$ -	-	-	-	-	-
29	$ 3	$ 4	-1	+1	2	+1
28	6	8	-1	+1	4	+1
27	9	12	-1	+1	6	+1
26	12	16	-1	+1	8	+1
25	15	20	-1	+1	10	+1
24	18	24	-1	+1	12	+1
23	21	28	-1	+1	14	+1
22	24	32	-1	+1	16	+1
21	27	36	-1	+1	18	+1
20	30	40	-1	+1	20	+1
19	33	44	-1	+1	22	+1
18	36	48	-1	+1	24	+1
17	39	52	-1	+1	26	+1
16	42	56	-1	+1	28	+1
15	45	60	-1	+1	30	+1
14	48	64	-1	+1	32	+1
13	51	68	-1	+1	34	+1
12	54	72	-1	+1	36	+1
11	57	76	-1	+1	38	+1
10	60	80	-1	+1	40	+1
9	63	84	-1	+1	42	+1
8	66	88	-1	+1	44	+1
7	69	90[1]	-1	+1	46	+1
6	72	90	-1	+1	48	+1
5	75	90	-1	+1	50	+1
4	78	90	-1	+1	52	+1
3	81	90	-1	+1	54	+1
2	84	90	-1	+1	56	+1
1	87	90	-1	+1	58	+1
0	90	90	-1	+1	60	+1

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[1] The indemnity would not increase for the additional lost bushel because the farmer has reached the maximum liability that he/she chose.

TABLE 5. FIFTEEN YEARS OF DRYLAND CORN YIELDS FOR INDIVIDUAL NORTHEASTERN KANSAS FARMS

Farm Num.	Years	Ave. Yd.	S.D.	Min Val.	Max Val.	C.V.	SKEW
23	15	112	38.1	11.5	152.8	33.9	-1.621
9	15	96	36.5	0.0	138.3	37.8	-1.354
7	15	56	26.6	0.0	88.3	47.9	-1.238
11	15	84	32.1	10.0	119.7	38.2	-0.950
51	15	90	38.0	6.5	145.0	42.4	-0.929
49	15	70	34.5	0.0	105.0	49.3	-0.851
3	15	87	31.4	10.0	130.8	35.9	-0.816
4	15	81	34.3	4.9	121.7	42.3	-0.776
41	15	95	23.4	44.0	123.0	24.6	-0.754
12	15	70	27.3	10.3	99.3	39.1	-0.727
43	15	67	31.7	0.0	107.0	47.1	-0.719
28	15	79	31.7	20.0	119.3	40.3	-0.702
6	15	71	35.4	3.5	115.0	49.5	-0.696
31	15	79	33.4	9.2	130.0	42.3	-0.693
32	15	78	42.6	0.0	136.3	54.5	-0.682
21	15	116	29.0	57.1	153.2	25.0	-0.656
2	15	91	40.2	10.4	139.9	44.1	-0.651
50	15	72	28.4	23.2	108.4	39.6	-0.642
45	15	74	29.6	8.0	121.6	40.2	-0.640
15	15	95	29.6	30.0	137.5	31.2	-0.611
25	15	80	38.3	8.8	130.2	47.7	-0.585
34	15	68	32.7	6.3	109.2	47.8	-0.567
36	15	77	40.5	0.0	148.0	52.5	-0.560
8	15	79	39.6	6.3	131.5	49.9	-0.544
5	15	97	33.4	22.2	146.0	34.6	-0.514
42	15	100	36.1	30.9	149.7	36.0	-0.514
40	15	103	30.5	31.4	155.0	29.7	-0.469
39	15	104	33.4	40.0	150.0	32.0	-0.462
33	15	104	32.6	43.1	144.8	31.5	-0.409
37	15	80	34.2	21.6	127.4	42.9	-0.399
29	15	88	43.6	20.0	142.0	49.5	-0.384
44	15	90	31.7	32.9	135.6	35.1	-0.380
48	15	69	33.3	5.0	110.0	48.2	-0.377
52	15	64	33.7	10.0	107.6	52.5	-0.328
30	15	83	35.0	21.7	137.5	42.3	-0.318
24	15	106	29.6	57.2	158.7	27.8	-0.318
26	15	84	32.0	25.0	130.0	37.9	-0.305
27	15	59	22.7	17.4	90.0	38.4	-0.299
20	15	62	23.9	13.6	106.0	38.4	-0.290
35	15	90	31.4	24.5	141.0	34.9	-0.279
10	15	121	37.9	64.0	176.0	31.3	-0.256
19	15	86	41.6	19.3	152.6	48.6	-0.234
46	15	79	34.6	19.3	137.7	43.8	-0.143
17	15	96	38.1	35.0	155.0	39.6	-0.118
1	15	57	27.4	6.5	100.5	48.0	-0.062
38	15	95	28.8	50.0	132.6	30.5	-0.039
13	15	62	36.2	10.0	125.8	58.1	-0.035
18	15	67	29.5	25.0	116.0	44.0	0.073
14	15	85	31.9	40.4	135.8	37.6	0.112
47	15	53	26.6	9.8	98.0	50.6	0.116
22	15	81	36.6	30.0	149.6	45.1	0.218
16	15	78	41.3	27.6	148.0	52.9	0.356

TABLE 4. TEN YEARS OF DRYLAND CORN YIELDS FOR INDIVIDUAL NORTHEASTERN KANSAS FARMS.

Farm Num.	Years	Ave. Yd.	S.D.	Min Val.	Max Val.	C.V.	SKEW
23	10	118	42.8	11.5	152.8	36.4	-2.061
42	20	115	33.8	30.9	149.7	29.4	-1.950
3	10	96	35.4	10.0	130.8	37.0	-1.738
33	10	116	31.7	43.1	144.8	27.3	-1.647
9	10	97	41.6	0.0	138.3	42.9	-1.614
11	10	88	34.9	10.0	119.7	39.7	-1.526
15	10	104	31.4	30.0	137.5	30.3	-1.519
29	10	103	43.4	20.0	142.0	42.0	-1.441
4	10	88	39.7	4.9	121.7	45.1	-1.436
7	10	56	31.0	0.0	88.3	55.8	-1.310
39	10	114	35.8	40.0	150.0	31.5	-1.310
41	10	104	19.9	60.0	123.0	19.1	-1.283
12	10	74	30.0	10.3	99.3	40.7	-1.283
28	10	84	35.0	20.0	119.3	41.5	-1.226
6	10	76	39.1	3.5	115.0	51.7	-1.125
5	10	103	39.1	22.2	146.0	37.9	-1.088
25	10	86	42.0	8.8	130.2	48.8	-1.081
21	10	124	28.5	73.0	153.2	23.0	-1.078
8	10	86	44.3	6.3	131.5	51.2	-1.072
44	10	98	34.4	32.9	135.6	35.0	-1.072
49	10	72	38.6	0.0	105.0	53.9	-1.055
43	10	70	36.0	0.0	107.0	51.6	-1.010
34	10	73	37.5	6.3	109.2	51.2	-1.007
32	10	84	47.1	0.0	13.3	56.0	-0.982
31	10	82	38.7	9.2	130.0	47.1	-0.967
51	10	91	41.3	6.5	145.0	45.5	-0.938
2	10	94	45.6	10.4	139.9	48.5	-0.932
35	10	98	35.1	24.5	141.0	35.9	-0.923
50	10	72	30.7	23.2	98.6	42.6	-0.906
24	10	114	30.5	57.2	158.7	26.8	-0.892
26	10	91	36.6	25.0	130.0	40.2	-0.838
30	10	89	40.3	21.7	137.6	45.4	-0.802
37	10	84	40.2	21.6	127.4	47.8	-0.780
48	10	73	34.6	5.0	110.0	47.4	-0.780
19	10	93	46.1	19.3	152.6	49.7	-0.725
18	10	74	30.0	25.0	116.0	40.5	-0.685
10	10	135	32.2	82.4	176.0	23.8	-0.676
38	10	105	27.6	56.0	132.6	26.4	-0.657
27	10	62	26.1	17.4	90.0	42.3	-0.628
17	10	109	35.9	52.0	155.0	33.0	-0.591
13	10	69	40.9	10.0	125.8	59.1	-0.518
45	10	71	33.3	8.0	121.6	46.8	-0.516
14	10	92	34.3	40.4	135.8	37.4	-0.415
1	10	64	30.2	6.5	100.5	47.2	-0.364
20	10	61	27.4	13.6	106.0	45.1	-0.343
46	10	81	38.1	19.3	137.7	47.2	-0.285
22	10	92	37.7	36.8	149.6	40.7	-0.280
52	10	65	36.6	10.0	107.6	56.4	-0.203
16	10	89	43.8	28.6	148.0	49.1	-0.157
36	10	86	45.5	0.0	148.0	53.0	-0.144
40	10	114	26.1	79.4	155.0	22.9	-0.102
47	10	50	30.4	9.8	98.0	61.0	0.335

Figure 1. Wheat
Impact of Price on Returns (Yield = 0)

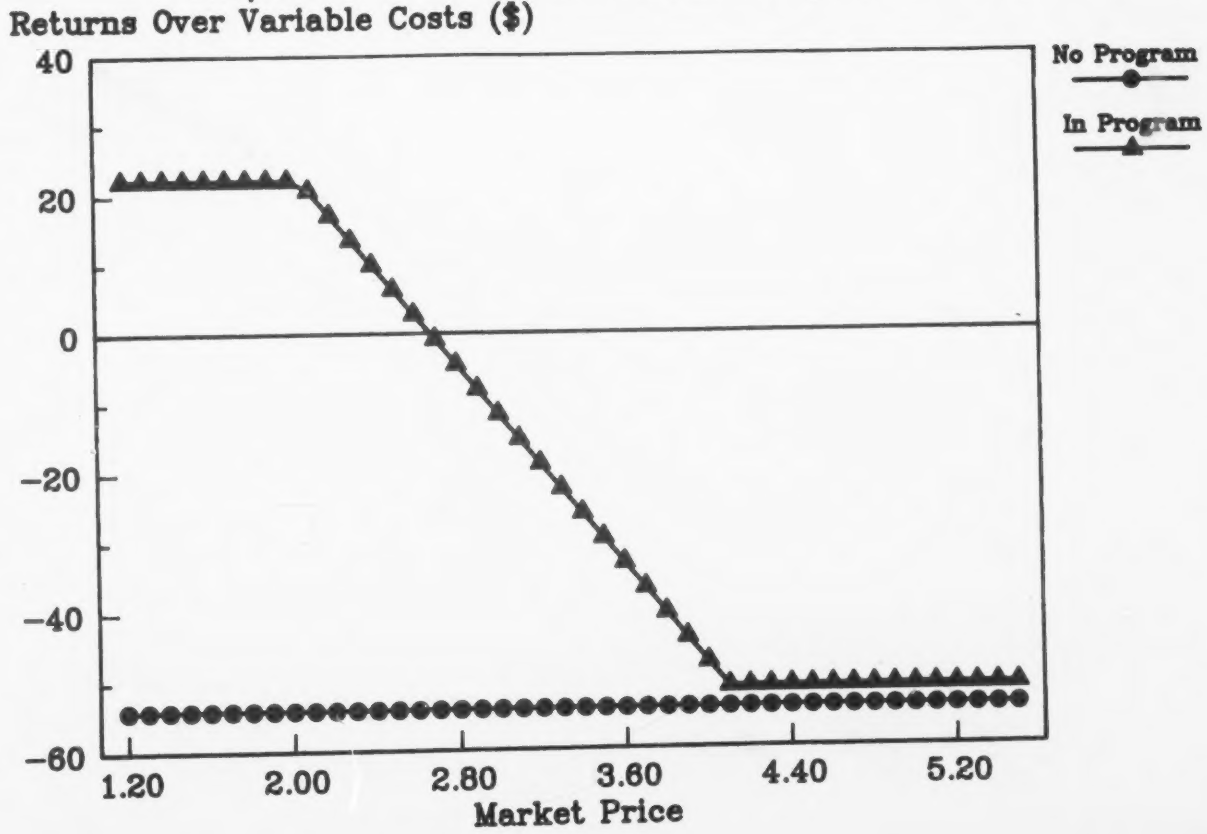
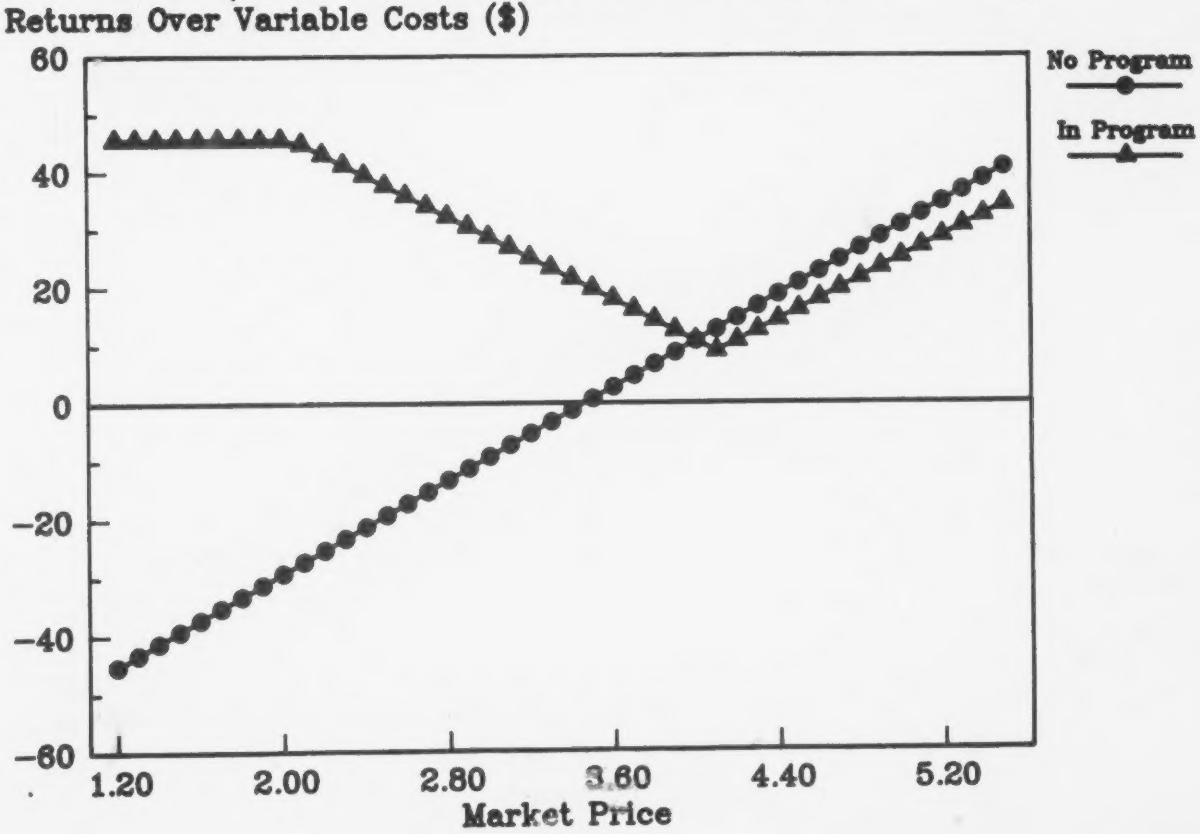


Figure 2. Wheat
Impact of Price on Returns (Yield = 20)



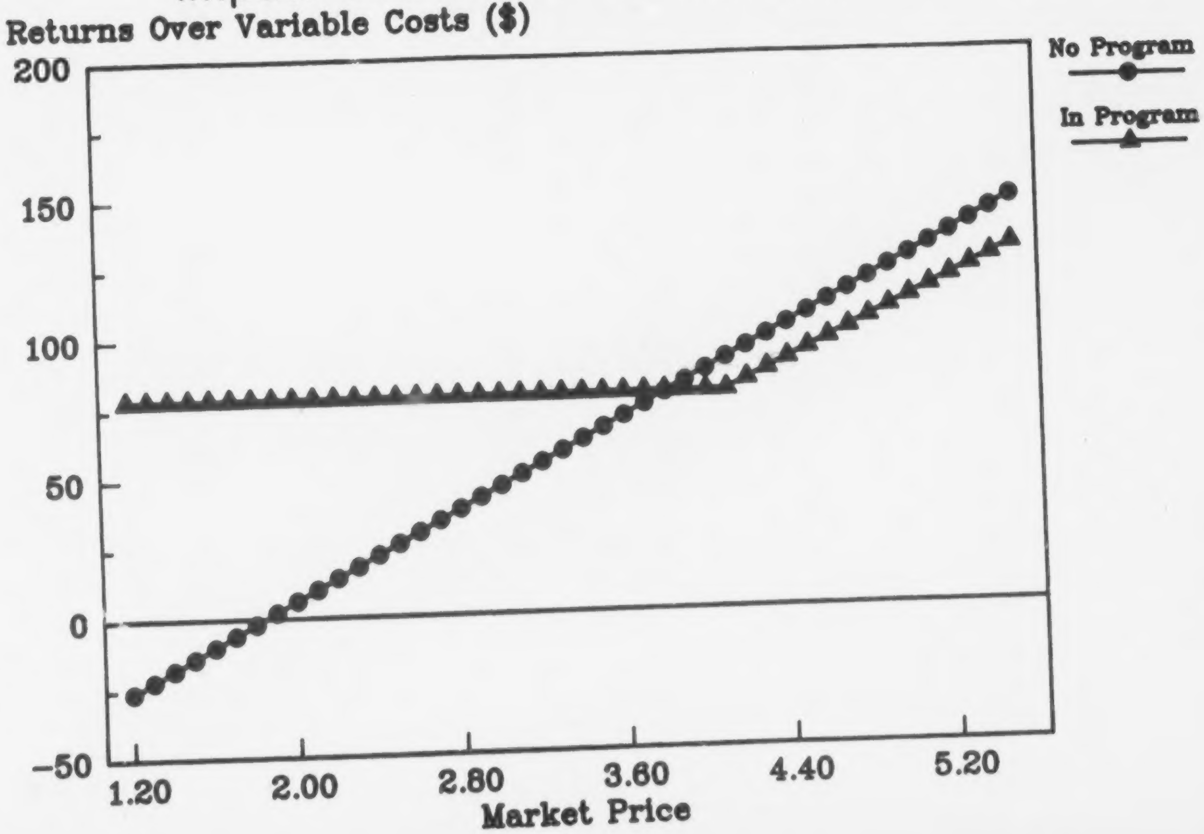


Figure 3. Wheat
Impact of Price on Returns (Yield = 40)

FIGURE 4. CURRENT MPCI(75%) AND DEFICIENCY COVERAGE OF PERCENTAGE REVENUE FROM WHEAT

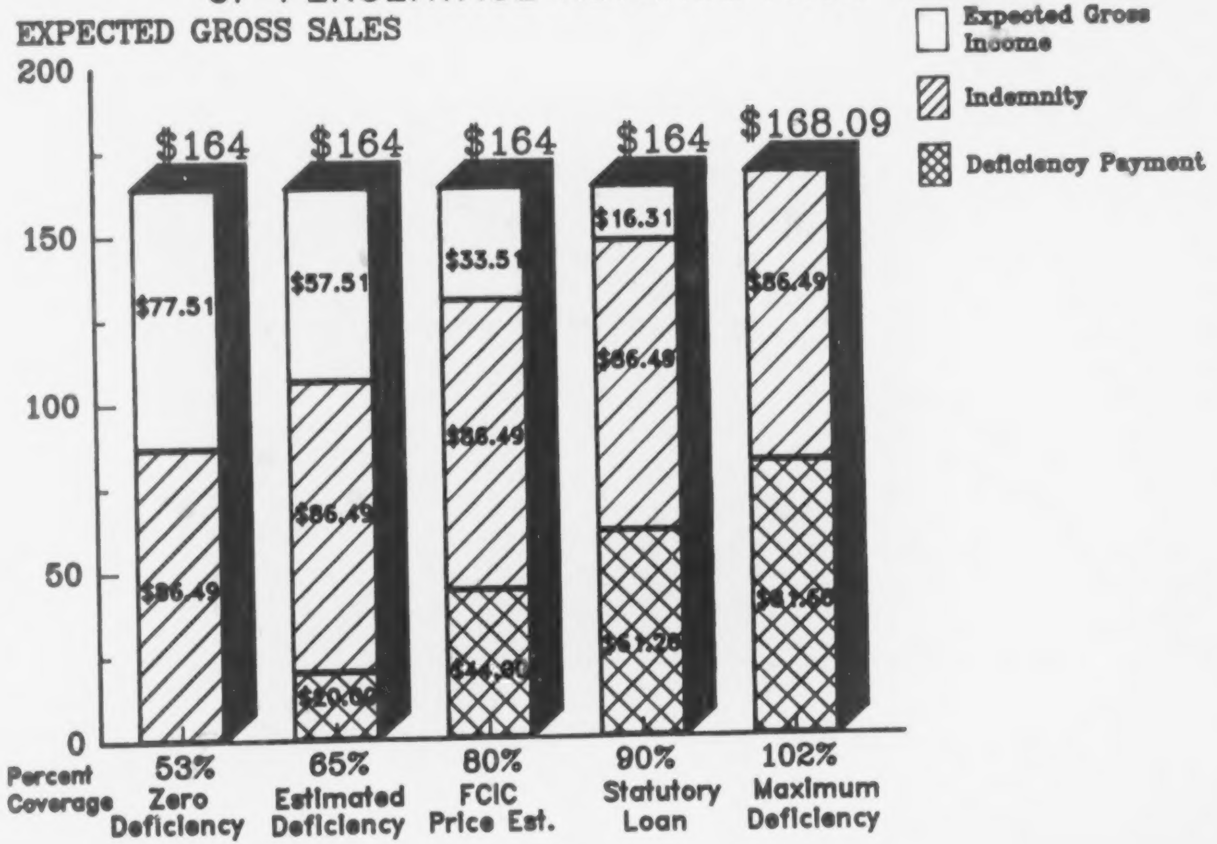


FIGURE 5. CURRENT MPCI(65%) AND DEFICIENCY COVERAGE OF PERCENTAGE REVENUE FROM WHEAT

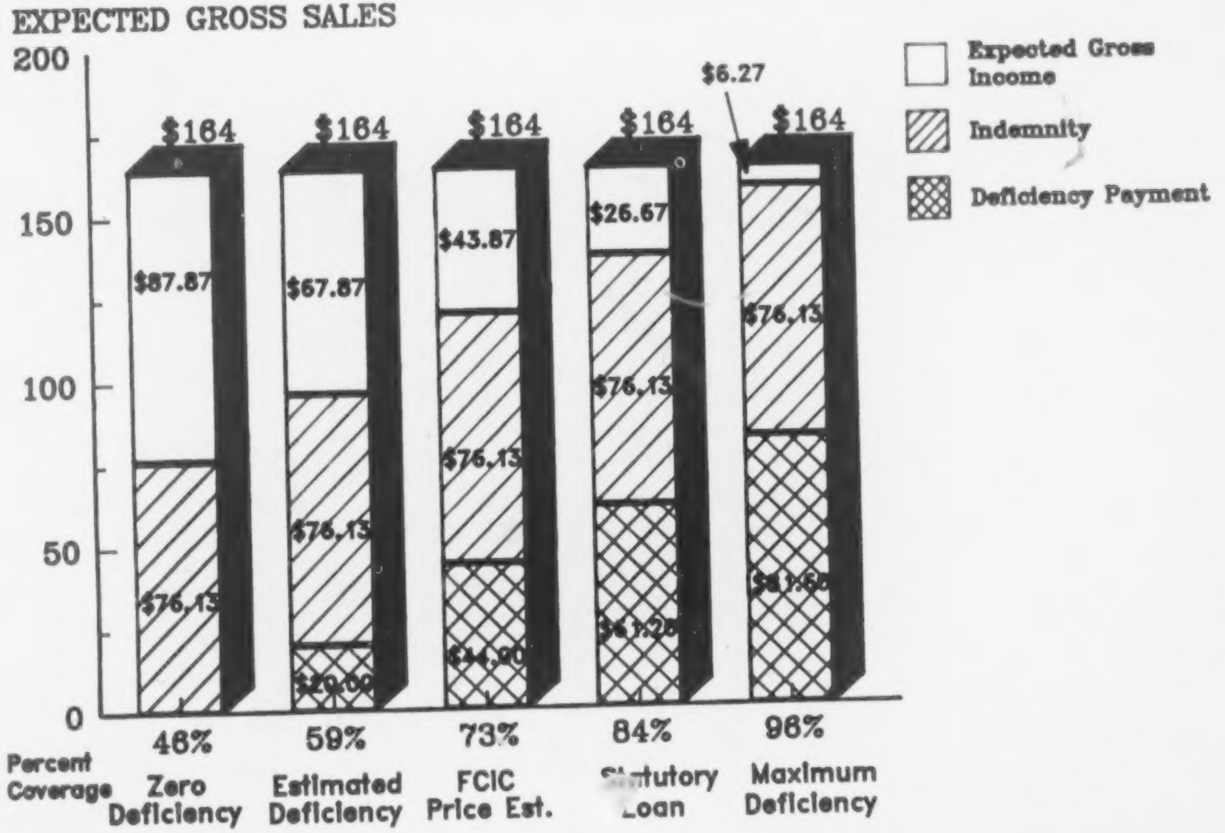


FIGURE 6. GROSS REVENUE BASED ON A $2.57 MARKET PRICE WITH A $3.00 AND $2.57 PRICE ELECTION

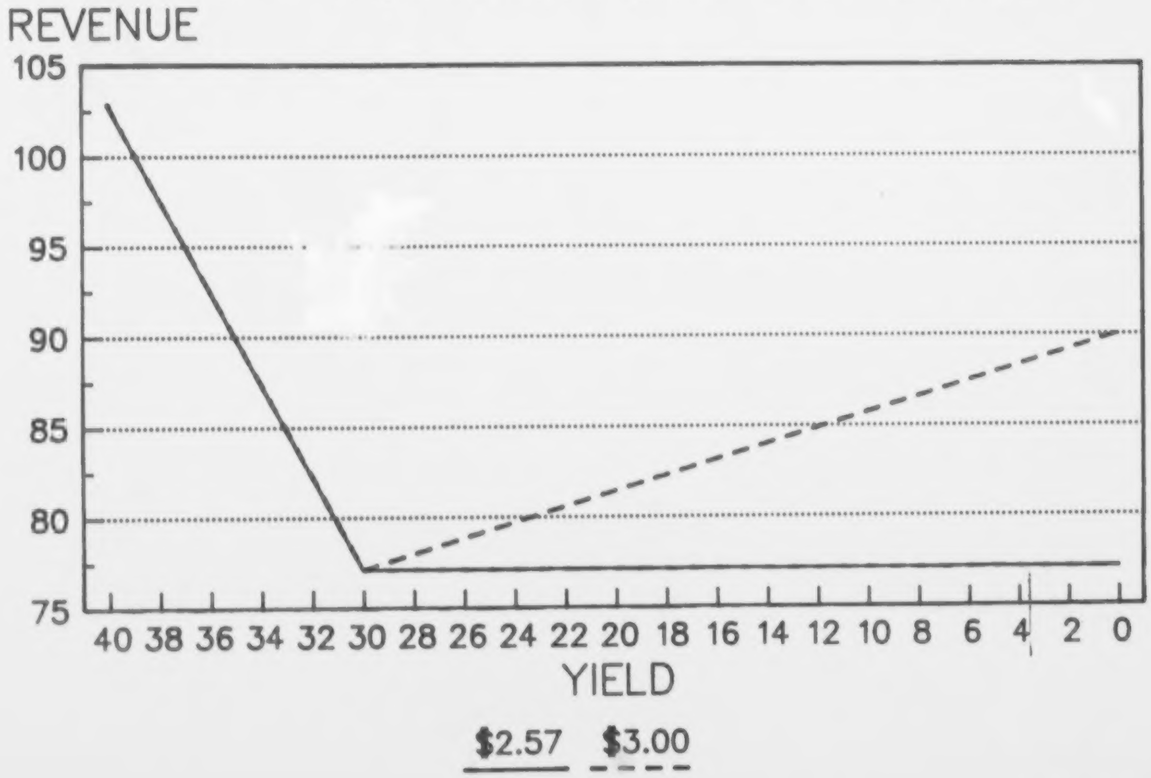


FIGURE 7. RETAIN ESTIMATED WHEAT DEFICIENCY PAYMENT VERSUS CURRENT PROGRAM

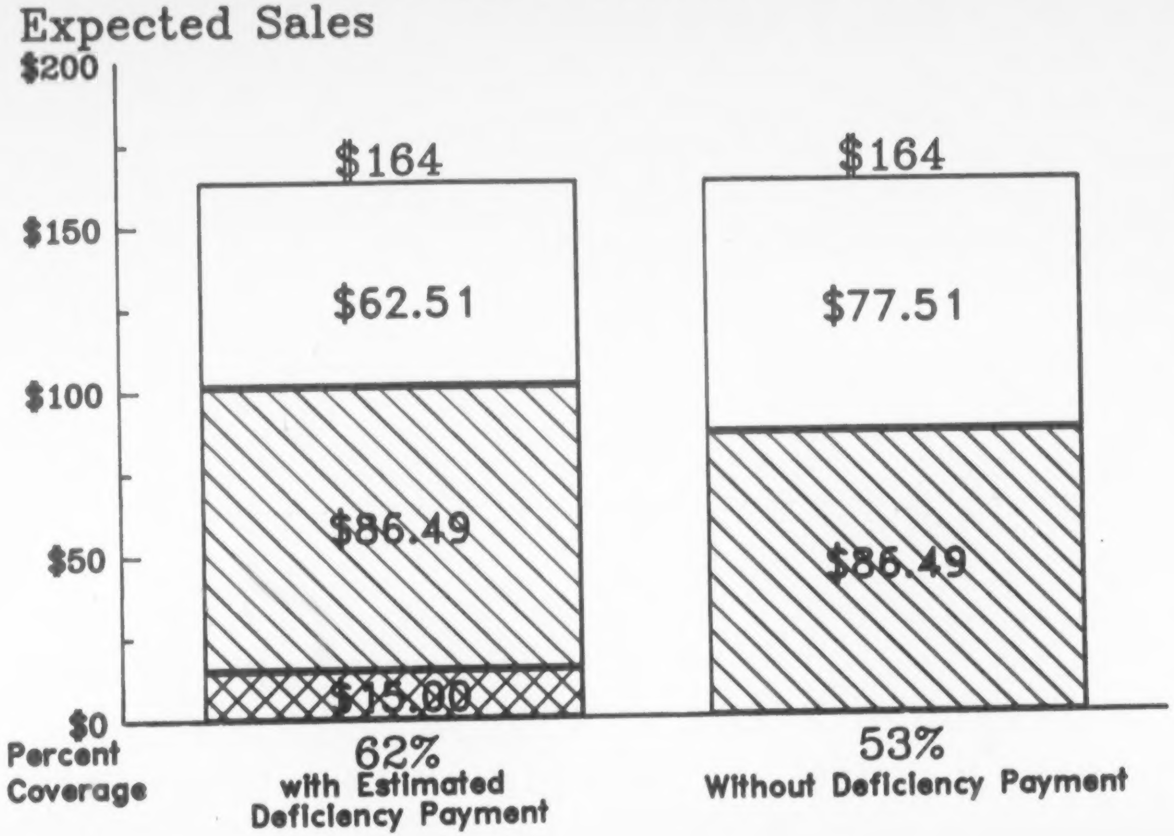


FIGURE 8. RETAIN ESTIMATED WHEAT DEFICIENCY PAYMENT VERSUS CURRENT PROGRAM

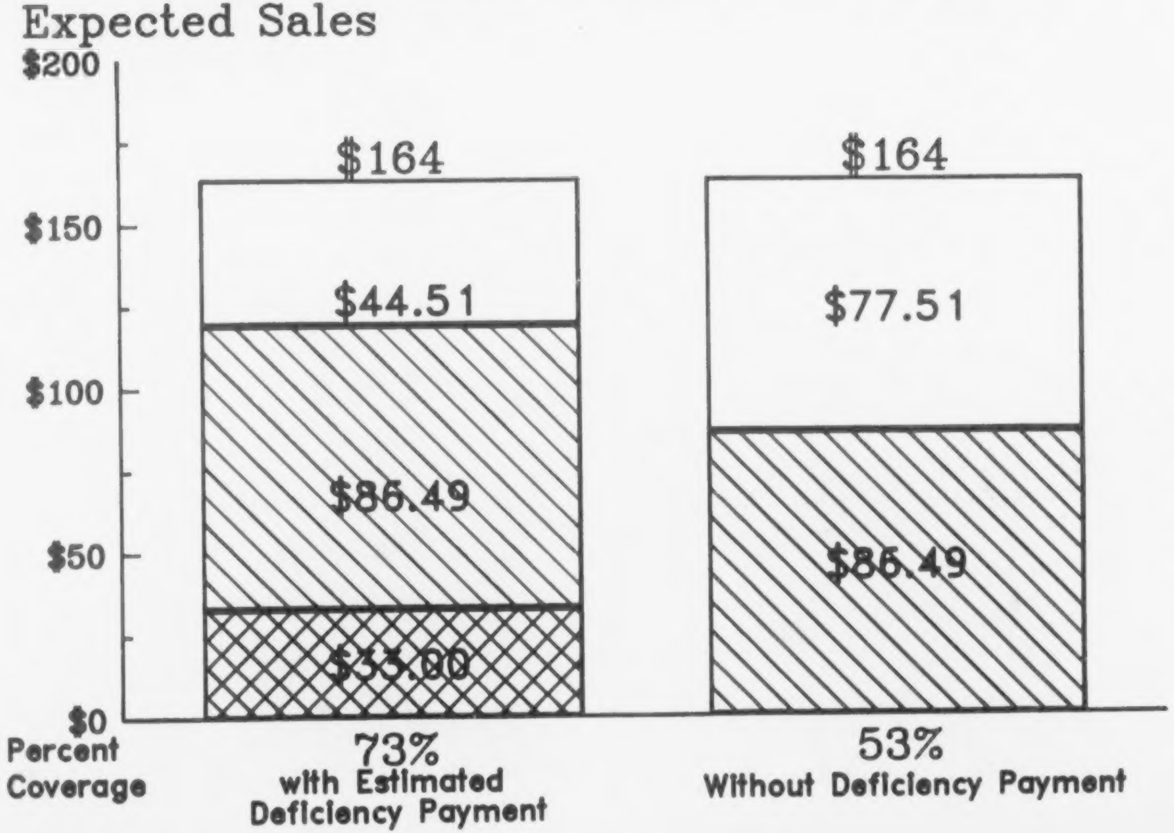


FIGURE 9. NORMAL DISTRIBUTION

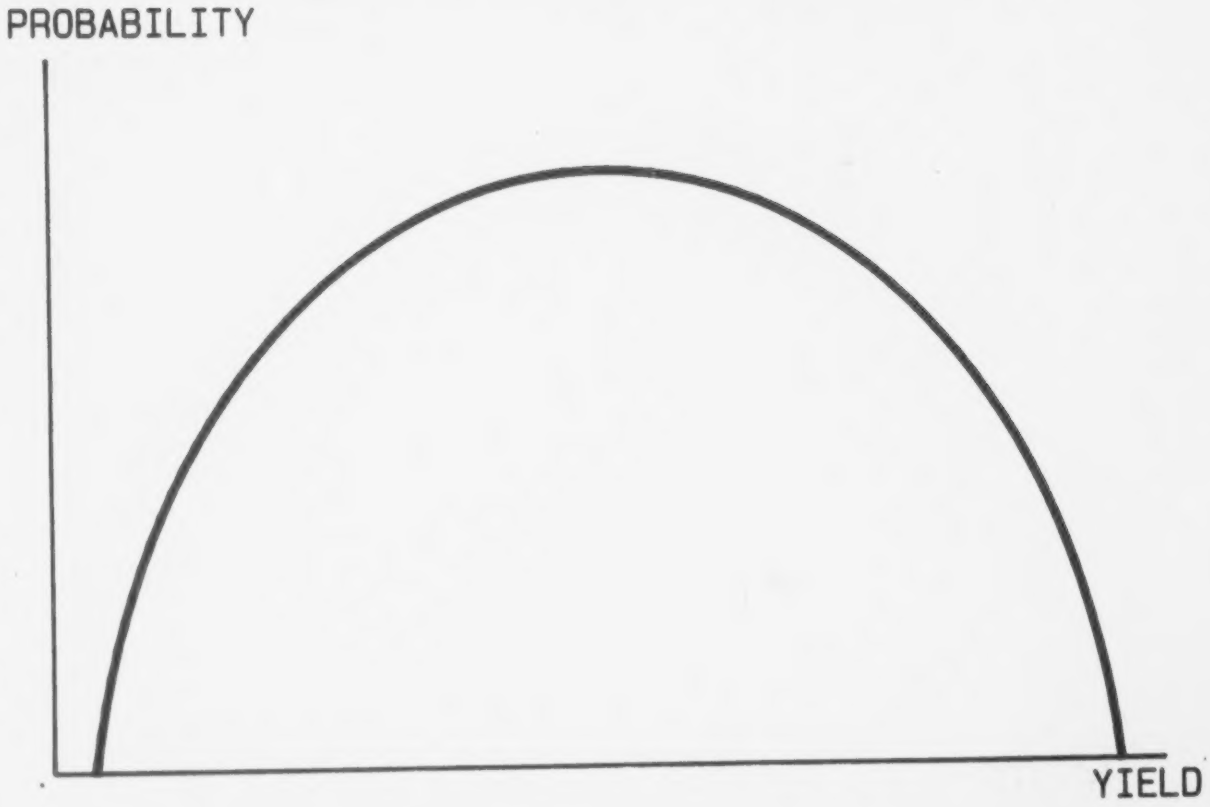


FIGURE 10. NEGATIVELY SKEWED DISTRIBUTION

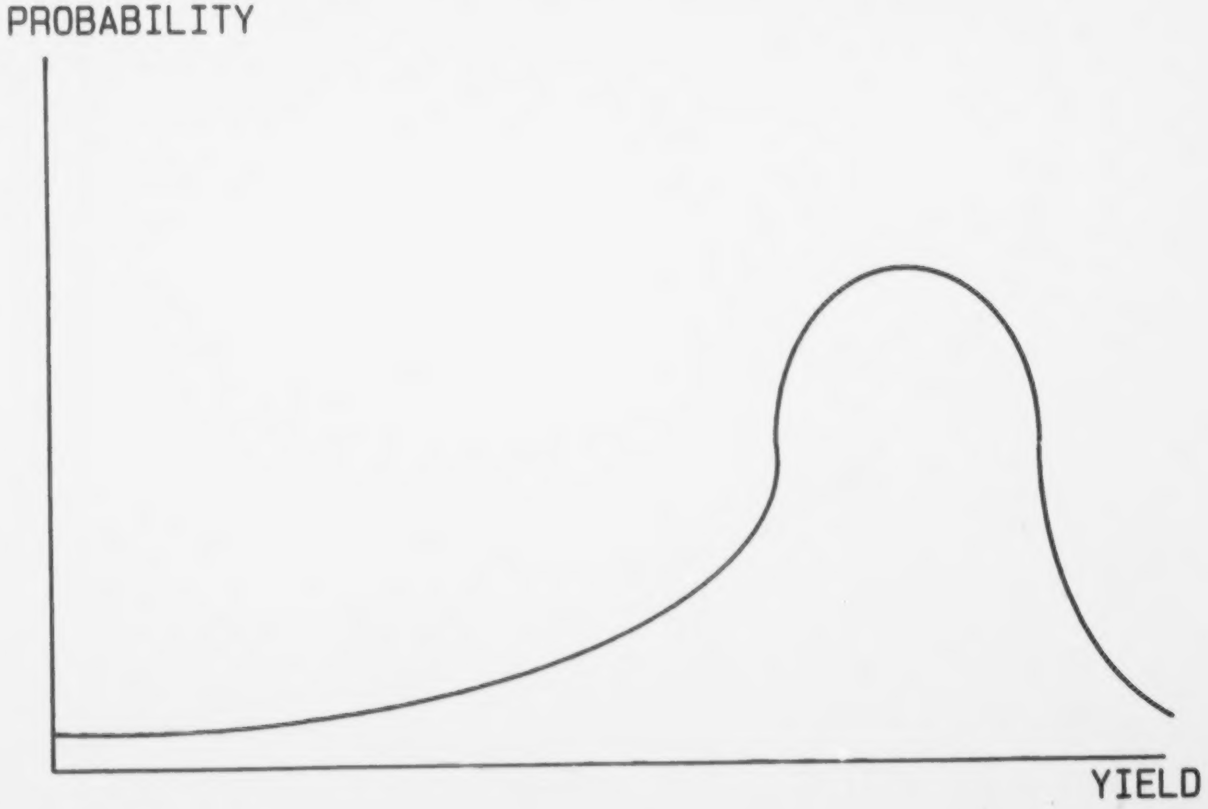


FIGURE 11. 10 YEARS OF CORN YIELDS

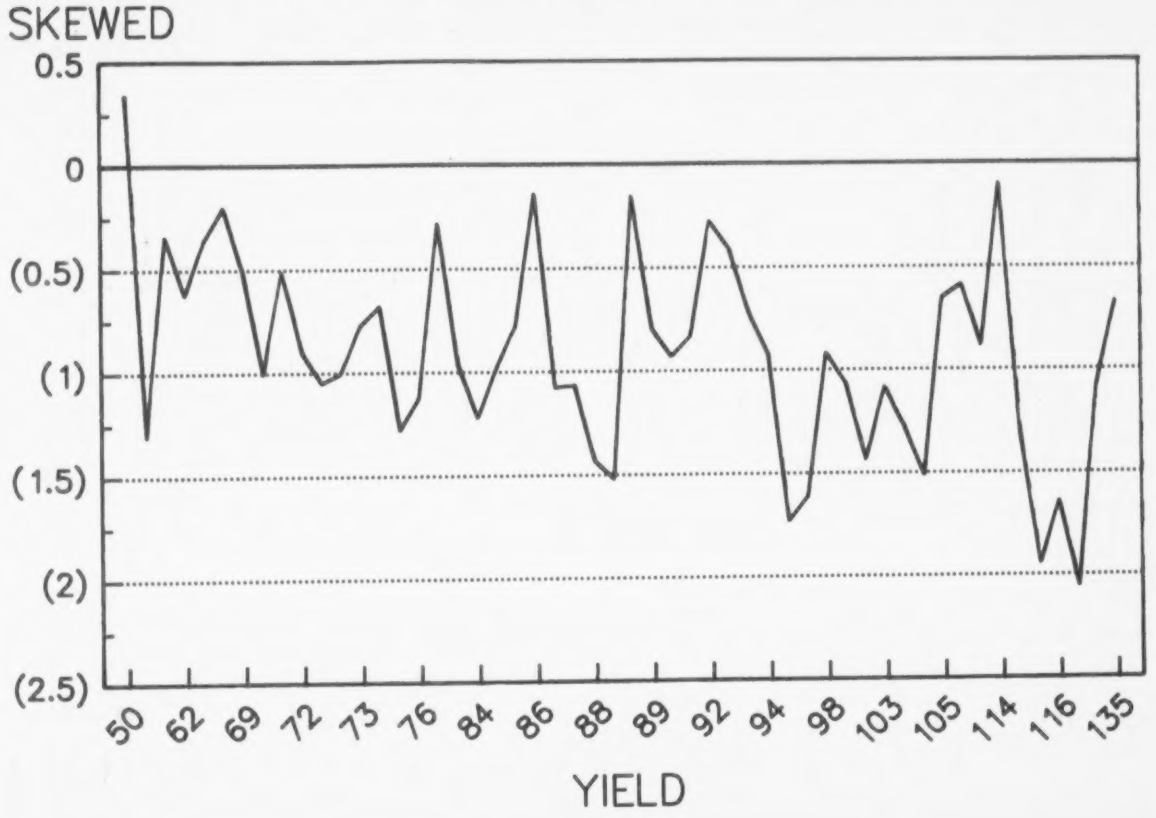
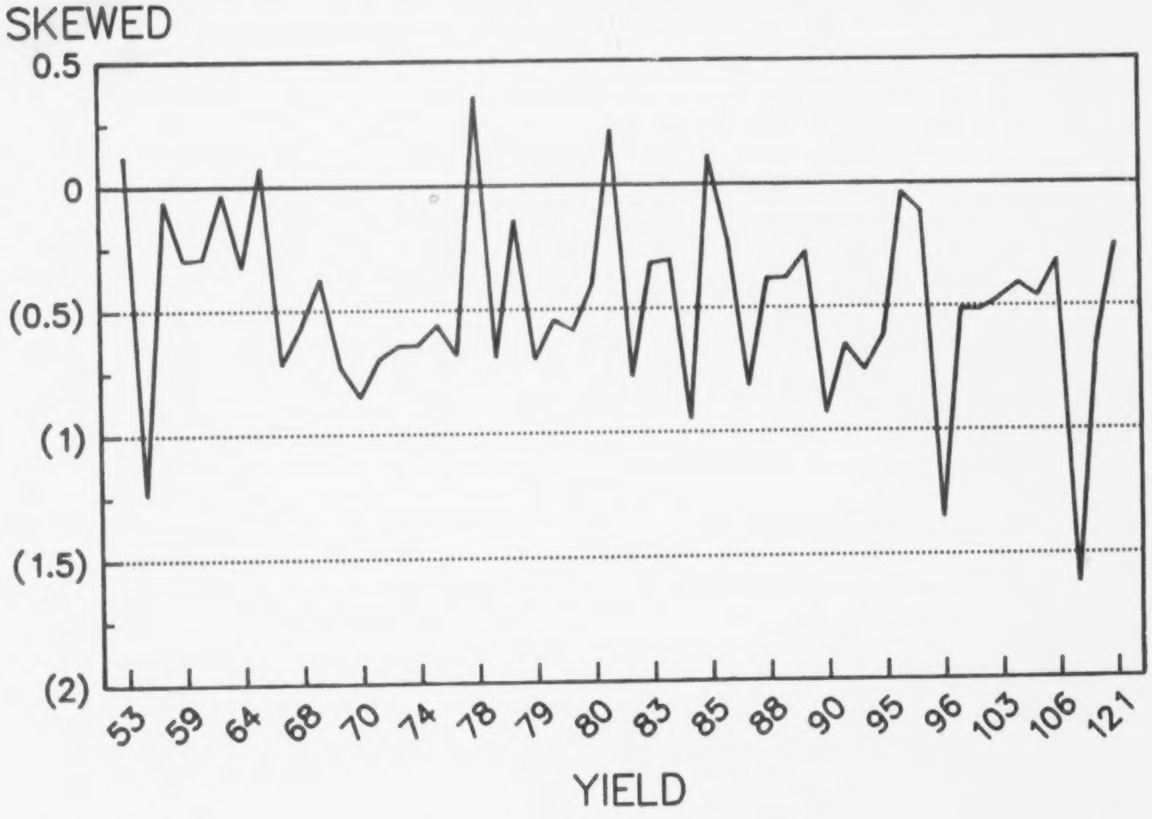


FIGURE 12. 15 YEARS OF CORN YIELDS



FIELD HEARING - DROUGHT EFFECTS IN KANSAS
by Larry Kepley - May 20, 1989

I appreciate the chance to be a part of this hearing along with the fine group of agencies and farm organizations who appeared before me. As a farmer and professional farm manager I have great respect for Sam Brownbeck and the leadership he is providing for Kansas agriculture. I watch Mike Smith's weather forecasts in hopes of rain almost every evening before I offer my prayers for his efforts. KSU's staff such as Jim Shoyer and Art Barnaby help us to understand and cope with drought. My farms were among the first to sign up with Servi-Tech and Rollie Stukenholtz when it was offered in Grant County.

Howard Tice of KAWG and Pam Dietz a fellow Farm Bureau member are champions of mine. By selling grain that goes to elevators that belong to Tom Tunnell's Kansas Grain and Feed Association I feel I belong to his group.

My neighbor, Homer Evans, being the National Lobbyist for AAM keeps me up to date on Jim Rice and AAM's strong efforts on behalf of better farming income.

As you see by my attached resume I am a "joiner" and the main reason I have not highlighted Don Lundquist, Paul Nauer and Tom Giessel and their fine farm organizations is that I have not been asked to join them. That will no doubt be corrected. As a good friend, Elmer Davis, who has served with me on other committees, I don't plant soybeans, but if you can find me some seed I may correct that oversite and thus be able to be a Soybean Association member. I use these opening remarks to reflect the perception of many of my fellow farmers who we all are here to try and represent. I hope to provide some common sense wisdom to the agriculture policy makers who have as much if not more control on our economic and social destiny as mother nature and fickle weather.

In 1988 I received Federal Crop Insurance payments and CCC disaster payments on some of my dryland wheat, hail insurance on some irrigated wheat and CCC disaster payments and Federal Crop Insurance on some of my irrigated corn that was hail damaged. Because of insurance availability and my management decisions I am still able to put out a crop in 1989. My farm net income for 1988 was barely on the profit side. Insurance is not designed to make money if collected and I fully understand that economic concept and concur with its intent. It would appear that 1989 will be the poorest I have ever experienced in wheat production and will be similar to yields in 1955 and 1936 to 1938 on our family farm. Drought and freeze have left our wheat stunted or dead. Small showers the past 3 weeks have given us minimum hope that we may get the irrigated milo to grow. We have not received enough to plant dryland milo and expect a harvestable crop.

Rain and snow effectiveness on our farm as in much of the High Plains is a function of total amount received for the growing season, but more importantly the individual event quantity, the amount that gets into the root zone and the number of heat units at critical growing periods. My dad has kept very detailed weather records for over 50 years and his father for some 50 years earlier. In 1988 we received 14.03 inches of moisture with 5 rains of just over 1 inch each. (Two in June & 3 in September)

From October 1, 1988 to May 1, 1989 (211 days) we had 1.35 inch of moisture with the most at one time of .40 inch. The July 1, 1988 to May 1, 1989 moisture was 7.64 inches. Dryland subsoil as well as surface moisture is nil.

I have faith it will rain and Western Kansas and the High Plains will bloom again.

Our efforts today are aimed at how best to survive with help from national policy implementation. Individual farmers for the most part are not in a very solid position economically nor are their financial backers (bankers, farm suppliers, or landlords) to come through the present weather crisis. They all have experienced the lingering severe economic period of the past 10 years that has left them with old machinery, tired older bodies, lower living standards than the bulk of their city customers, and for many a very pesimistic attitude. We have no savings or income reserves to fall back upon to get out the next crop. The May 14, 1989 Wall Street Journal says that 40% of the farm belt is threatened by this years drought.

What is needed --

A. The 1985 Food Security Act was a very comprehensive effort by agriculture policy makers to address the needs and wants of consumers, federal budget makers, politics, foreign markets, ecologists, agri-businesses, financial institutions and maybe not least the american farmers. There continues to be refinements of the original act. I believe with implementation of laws in place and some added refinement legislation disaster and drought relief can better be provided to agriculture.

As near as I can determine the cost of production studies that are used to partially base the target prices of grain do not consider an allowance for risk of a natural disaster either as commercial crop insurance premiums or as a self insurance risk factor. The target prices were set in 1985 based upon 1984 and earlier cost of production levels and are outdated. The target prices have been reduced since 1985 for reasons that had no economic relation to grain production costs.

According to the S.W. Kansas Farm Management Association figures gathered from dryland wheat farms the cost of wheat production has gone from $55.15 per acre in 1986 to $72.22 per acre in 1988. The average production in 1986 was 30.8 bushels per acre, 1987 was 36.1 bushels and 1988 was 26.5 bushels. 1989 average production will be less than 20 bushels per acre, but with little if any reduction in production costs. I need to define that the Kansas Farm Management Association costs quoted here do not include an allowance for risk, operator labor, land return or management return which are all valid inputs to production.

I believe target prices need to be increased to reflect more realistic grain production costs.

The 1985 act as implemented encouraged farmers to carry Federal Crop Insurance on 65% of their share (30% USDA subsidized) through commercial insurance carriers. For many reasons this has been a poor solution in relation to the old CCC disaster programs. It has created a host of paper shuffling, check and re-checking. It has been a most inefficient delivery system for a well intended program.

This year eight landlords and I have Federal Crop Insurance. Each contract has to have a CCC AD1026, last years crop production, individual application, individual premium notes and a year end proven production report filed if there is no claim. Last year when I had a claim I had field inspections three times (Farm Bureau Insurance, OMB, and Farm Bureau Insurance) and four trips to the local ASCS office and the Farm Bureau Insurance office to settle the claim.

The old CCC disaster program required one inspection and a production claim form to be filed. The old system was much more efficient than the Federal Crop Insurance - Disaster Program Combination. I think the old system should be back in the 1990

Farm Act.

B. Continue the 1988 disaster program for crops grown or planted in 1989. While it is cumbersome and is delivered rather inefficiently it is generally perceived as national budget affordable.

C. Try to maintain grain stocks under loan in a broad base of storage facilities as possible to give storage income to local facilities and to be available for needed livestock feed in areas under drought stress.

D. Expand drought feed and grazing allowances to farmers and ranchers who qualify and need this help as soon as possible. Every days delay means backward gain, stunted calves and poor fertility cows.

E. Expand FHA disaster loan funds to help those farms that can qualify.

F. Expand SCS and Rural Water District programs and funds or redirect existing funding to develop agricultural and domestic water supplies in drought areas.

G. Federally fund expansion of the Western Kansas Muddy Roads rain enhancement and hail suppression cloud seeding project.

H. Ask the Federal Energy Commission to help irrigators using natural gas to pump water to be able to buy it at affordable prices. FERC Orders 451 and 436 as implemented by the gas companies have caused natural gas to be priced so high that irrigation has been curtailed in many High Plains areas. H.R. 658 passage may also give some price relief to farmers.

Thank you for this time. I will be very receptive to questions or a chance to expand upon these remarks at a future date.

(Attachment is held in the committee files.)

COOP

GARFIELD COOPERATIVE
Hwy. 56 — P.O Box 198
GARFIELD, KANSAS 67529

Phone (316) 569-2266
or (316) 569-2267

May 24, 1989

REF: Additional Written Testimony for Field Hearing held in Great Bend May 20, 1989.

Honorable Dan Glickman
Chairman House Ag.Sub. Comm. Wheat- Soybeans- Fall Crops

Honorable Ron Marlenee
Vice-Chairman House Ag. Sub Comm. Wheat-Soybeans-Fall Crop
1301 Longworth Off Bldg.
Washington, D. C. 20515

Dear Sirs:

To insure planting flexibility, producers combine both irrigated and dry land farm ground together as one unit when dealing with government farm programs. These acres are than called a farm and carries a base for plantable acres as a whole and not as each individual piece of ground. This allows the producer to plant his farm base for optimum farm management. Without this option he would find irrigated, circles partially planted causing idle acres to be irrigated providing only weed potential. The flexibility allows him to plant full circles of wheat and idle dry land.

Our request is that when applying and receiving drought assistance that this be on a Field- by- Field basis and not by ASCS definition of FARM UNIT. This would allow the dry land to stand on it's own merit and the irrigated to stand on it's merit. We are concerned that if this is not done, those producers who have chosen flexibility will be penalized. The economic loss of zero production on their dry land acres will be over shadowed by their irrigated produced bushels (which will be smaller than normal); giving them the potential placing of being placed out of the drought relief standards. Placing each field on it's own production will be more equitable to the Producer.

Cordially yours,

Kim Alan Barnes

Kim Alan Barnes
General Manager

c.c. Rep. Dan Glickman
c.c. Rep. Pat Roberts

AGRICULTURE
CONGRESSMAN DAN GLICKMAN, CHAIRMAN
CHAIRMAN: SUBCOMMITTEE ON
WHEAT, SOYBEANS,AND FEED GRAINS
Hearing
Great Bend, Kansas May 20, 1989
by
Don Christy of Ag Management Service

Mr. Chairman, and members of the subcommittee, I am Donald Christy, with a long history of presenting THE MERITS OF THE HIGH PLAINS and its productive capabilities.

RESUME':

I recommend that the present drought disaster law be extended to include the crops of 1988 and include the fall seeded 1990 crops. The rewards for efficient food production should be high enough to encourage some farm boys to want to be farmers. In the 1960's my two boys ask, why work so hard for such small rewards. Agriculture is suffering a serious economic adjustment period. It is still less rewarding than it was in the 1960's. There are a few young operators that still have a chance to continue farming.

A young renter, farming 1600 acres of wheat and milo, under the present government acreage limitations could expect to make about $ 5200 per year without government payments per farm worker. This is based on normal yields and wheat and milo price at $2.60 and $1.85 per bushel respectively. This is far below the poverty level. However, the 1987 $7,000 government payment gives him a $12,000 a year income. Hardly, an attractive reward for his efforts. My calculations indicates a probable one year $28,000 loss if both crops fail and he is not insured.

The all peril crop insurance could be an attractive service to the farm operators. One of the problems is, if the yield equals the insured level, the expense of the harvest and the insurance premium still has to be to be paid. If he was insured and had a complete wheat failure but a normal milo yield, his loss would have been over $2,000. A complete milo failure and a normal wheat yield would indicate $5,200 income. If the Milo yield was at the insured level and he harvested and sold it, his income would have been less than $1,000. It is interesting to note that If the Government had paid for the harvest and took the milo, the milo would have cost the government less than $1.60 per bushell.

The another insurance problem is that the ten year yield must be proved or a much lower yield is used to calculte a higher premium and a lower settlement payment payment (see TABLES I, & II). Our insurer gave us the yield level of .82 x the county yield for summer fallow wheat and .86 for dryland milo. Our insurance agent says, that less than 40 percent of the insured have been able to provide the proof of the 10 year yield.

DISCUSSION:

DISCUSSION:

The bibical reference to the 7 fat years and the 7 lean years is well recorded. I heard Dr. Bennett, director of FAO, after he left Oklahoma A. & M., say "the greatest famine in history, in which some 10 million Chinese died, was a failure. There was more people when the famine ended than when it began". The of yield and price in the 1930's and 50's and the Russian need for food in the 1970's suppports the concept that small surpluses and small shortages bring wide changes in price. A farmer can only plant and pray. I other words economically speaking that makes these commodities "soft commodities". Consequently, a farmer survives longer by producing at a loss than if he were to close down. It is almost impossible, except for the owner operator, to again start farming, after closing down.

ANALYSIS OF THE MERITS OF INSURANCE

Table III was recorded from the Kansas State Board of Agriculture reports. It was centered around Scott County. A program was written to aid in the calculation of the expected returns to the owner operator, the renter, and the land owner. The income and losses were calculated for normal USDA ASCS yields for summerfallow wheat and dryland milo production. The income and expenses were expanded to 5 times the half section income and expenses. The realestate property tax was included. The custom farm operations rates were used to obtain the costs of the farm operations. I had been farming on the custom rate basis using the Kansas State Board of Agriculture reports as the basis for obtaining the needed services. I found it workable.

The young renter faces a tough prospect for success. A $5200 average annual income with the potential loss of more than 5 times the annual income. However, the loss with the mid rate insurance and price B resulted in a loss of less than 1/10 the annual income. It is interesting to note that the renter had the same income with an insured complete milo failure as he had for both crops insured and with normal crop yields. If the yield had equalled the insured yield the harvest and haulling would have cost about the value of the insurance. In other words the harvest cost would about equal the income due to as complete milo loss.

TABLE I SCOTT COUNTY SUMMERFALLOW WHEAT COVERAGE AND RATE.

ST: KANSAS [20] CO: SCOTT [171] CROP: WHEAT [11]

APPROVED APH YIELD	CLASSIFICATION	SUBSIDIZED PREMIUM RATES		BASE PREMIUM RATE	MAX REDUCTION FOR EXCLUDING HAIL AND FIRE PROTECTION
		WITH HAIL AND FIRE PROTECTION (PERCENT)	WITHOUT HAIL AND FIRE PROTECTION (PERCENT)	(PERCENT)	(PERCENT)
				PRACTICE: Summerfallow [005]	
(BU.)		COVERAGE LEVEL 1 (50%)			
14 & Below	R1	18.6	15.3	26.6	4.7
15 - 18	R2	15.3	12.0	21.9	4.7
19 - 23	R3	11.1	7.8	15.9	4.7
24 - 27	R4	8.5	6.0	12.2	3.7
28 - 32	R5	6.9	4.8	9.8	2.9
33 - 36	R6	5.7	4.0	8.2	2.5
37 - 41	R7	4.9	3.4	7.0	2.1
42 - 45	R8	4.2	2.9	6.0	1.8
46 & Above	R9	3.9	2.7	5.6	1.7
		COVERAGE LEVEL 2 (65%)			
14 & Below	R1	25.8	22.0	36.9	5.5
15 - 18	R2	21.2	17.9	30.3	4.7
19 - 23	R3	15.4	12.1	22.0	4.7
24 - 27	R4	11.8	8.5	16.9	4.7
28 - 32	R5	9.5	6.7	13.6	4.1
33 - 36	R6	7.9	5.5	11.3	3.4
37 - 41	R7	6.7	4.7	9.6	2.9
42 - 45	R8	5.8	4.1	8.3	2.5
46 & Above	R9	5.5	3.9	7.8	2.3

TABLE II 1989 PRICE ELECTION.

	A	B	C
CORN (41) type 290	1.50	2.00	2.60
SOYBEANS (81)	5.00	5.50	6.17 M.P.
GRAIN SORGHUM (51)	1.50	1.85	2.40
SUNFLOWERS (78) non-490 oil-480	.07	.08	.09
OATS (16)	.90	1.10	1.25
BARLEY (91)	1.10	1.30	1.60
SUGAR BEETS (39)	18.00	30.00	35.00
POTATOES (84)	3.50	4.50	4.75
POPCORN (43)	.09	.10	.12
WHEAT (11)	2.25	2.60	3.00
DRY BEANS			
PINTO (M610)	.10	.12	.15
SMALL WHITE (R610)	.18	.24	.30
LIGHT RED KIDNEY (H610)	.18	.24	.30
PEA (K610)	.16	.20	.24
GREAT NORTHERN (G610)	.10	.13	.17
PINK (L610)	.10	.13	.17

TABLE III SUMMERFALLOW WHEAT AND DRYLAND MILO YIELDS OF CENTRAL
WEST 1/3 OF KANSAS.

							AV.									AV.									AV.
SHERMAN	21	19	17	20	36	33	26	21	36	35	29	26	36	31	33	31	39	21	36	45	47	52	34	30	39
WALLACE	12	10	1	17	27	27	16	15	24	32	20	27	33	31	26	26	34	17	42	45	45	42	27	37	36
GREELEY	7	3	1	20	35	30	16	19	25	34	24	19	19	32	29	25	30	17	24	39	41	40	20	36	33
HAMILTON			2	21	36	31	23	22	23	27	20	17	22	27	26	23	31	20	25	36	39	37	27	35	31
STANTON	9	2	1	16	21	21	12	14	24	23	16	22	26	21	32	22	35	15	24	41	36	33	23	31	30
NW AV.	12	8	4	20	31	28	18	18	26	30	22	22	27	28	29	25	34	18	30	41	42	42	28	36	34
THOMAS	17	19	10	25	34	33	23	30	37	35	31	36	35	36	44	36	44	12	36	45	40	59	39	37	39
LOGAN	13	19	7	25	29	31	21	24	32	25	27	35	33	33	40	31	37	15	26	43	44	50	32	36	35
WICHITA	10	13	2	20	32	30	19	23	26	33	20	19	21	31	26	26	33	12	31	44	47	43	35	40	36
KEARNY	5	7	8	20	29	31	17	28	28	32	25	19	28	31	31	28	30	16	32	33	41	37	37	30	33
GRANT	4	10	2	27	31	22	16	24	29	26	20	23	33	23	36	27	33	20	33	46	39	37	37	39	35
SCOTT	11	22	7	30	36	28	22	27	37	32	31	26	32	36	38	32	40	19	35	49	46	40	34	40	38
FINNEY	13	11	6	32	30	36	21	34	33	33	28	25	29	34	34	31	32	11	35	46	34	30	26	40	33
HASKELL	5	5	6	33	26	34	18	35	42	32	25	23	29	27	33	31	33	16	35	37	41	40	34	36	34
WC AV.	10	13	6	27	31	31	20	28	33	31	27	26	30	31	35	30	35	15	33	43	42	43	34	38	35
SHERIDAN	19	21	17	26	32	38	26	32	40	33	35	35	30	34	43	35	39	16	46	47	35	53	34	42	39
GOVE	13	25	9	30	32	32	24	32	40	31	37	39	32	32	38	35	41	17	32	50	46	50	30	43	38
LANE	9	20	6	30	34	31	22	35	40	35	32	30	31	35	39	35	38	11	35	43	40	41	28	43	35
GRAY	9	12	8	32	33	34	21	38	39	30	30	25	31	24	40	32	34	16	41	46	40	38	33	40	36
WC AV.	13	19	10	30	33	34	23	34	40	32	34	32	31	31	40	34	38	15	38	46	40	45	31	42	37
GRAHAM	18	23	19	25	30	35	25	34	39	26	31	33	29	27	39	32	38	19	36	43	37	36	29	41	35
TREGO	15	22	9	25	33	30	22	35	38	25	32	33	31	27	35	32	35	20	36	40	40	43	26	44	35
NESS	10	13	8	33	35	26	21	32	40	27	29	33	32	30	30	32	39	16	39	45	38	37	23	40	35
FORD	11	15	13	35	35	30	23	36	37	26	30	31	28	21	39	31	27	21	36	40	41	33	38	30	34
SW AV.	13	18	12	29	33	30	23	34	38	26	31	32	30	26	36	32	35	19	37	42	39	37	29	41	35
AREA AV.	12	15	8	27	32	31	20	28	34	30	28	28	29	30	35	30	35	17	34	43	41	42	31	39	35
							AV.	WEST THIRD KANSAS DRY LAND MILO YIELDS LESS N & S ROWS								AV.									
SHERMAN	34	22	17	30	24	24	25	34			21	26	52	21	51	34	38	49	56	32	35	47	32	41	41
WALLACE	10	22	16	26	23	21	20	32	43	40	20	20	45	30	38	33	38	42	38	30	37	42	43	44	39
GREELEY	28	21	10	31	25	16	22	36	30	31	30	20	30	29	33	30	37	30	25	21	30	37	36	36	33
HAMILTON		19	10	32	34	31	25	31	30	16	20	17	22	27	26	24	23	46	20	21	30	34	43	37	32
STANTON	20	19	10	23	24	18	19	34	34	36	23	24	26	22	22	28	20	34	19	16	28	26	36	32	27
NW AV.	23	21	13	28	26	22	22	33	34	31	23	21	35	26	34	30	33	40	32	24	34	37	38	38	34
THOMAS	31	23	18	33	31	32	28	54	42	33	35	30	51	38	53	42	44	56	40	40	56	59	41	60	41
LOGAN	27	18	19	24	24	21	22	35	40	37	40	25	50	25	47	37	40	40	39	30	51	56	36	54	43
WICHITA	26	21	16	26	31	24	24	34	34	18	25	22	42	38	33	31	54	32	32	22	45	47	47	51	41
KEARNY	30	21	15	38	40	31	29	52	49	22	28	17	33	35	36	34	41	45	36	24	41	47	54	38	41
GRANT	24	19	15	40	33	30	27	42	37	32	24	22	33	30	32	32	37	36	28	18	34	38	39	30	32
SCOTT	27	21	20	31	31	34	29	48		20	27	24	51	34	50	36	45	40	49	18	34	49	36	53	42
FINNEY	24	22	21	31	33	33	27	48	45	18	26	21	47	8	40	33	38	47	45	20	34	45	40	40	41
HASKELL	15	24	14	29	33	27	24	49	45	39	20	24	34	33	34	35	30	67	23	14	42	44	54	45	40
WC AV.	25	21	16	30	29	26	24	40	39	29	26	22	39	28	38	33	37	44	35	24	39	4[illegible]	42	43	38
SHERIDAN	35	24	31	32	35	35	32	51	48	30		29	66	29	53	44	39	51	47	31	52	61	49	69	50
GOVE	32	20	32	36	31	35	31	51	54	29	40	27	67	36	47	44	47	50	46	20	46	41	37	66	44
LANE	32	21	20	38	32	32	29	59	48	25	31	26	51	24	52	39	45	40	37	21	37	40	41	62	41
GRAY	45	20	16	32	34	41	31	41	41	39	24	19	36	31	45	35	35	54	40	22	35	44	49	56	42
WC AV.	36	21	25	34	33	36	31	50	48	31	32	25	55	30	49	40	42	51	43	23	43	47	44	63	44
GRAHAM	31	21	25	36	34	28	29	40	40	27	27	29	54	32	55	39	29	42	43	17	34	43	41	67	40
TREGO		20	22	34	23	28	25	46	50	29			55	30	53	44	43	52	44	14	38	43	35	64	42
NESS	29	18	25	32	23	29	26	47	38	20	26	25	47	22	46	34	42	46	37	18	29	37	39	62	39
FORD	28	20	20	40	20	30	28	45	35	21	20	24	41	33	45	33	40	52	34	29	43	49	58	61	46
SW AV.	29	20	23	35	27	29	27	46	41	24	24	26	49	29	50	36	39	48	40	20	36	43	43	63	42
AV OF YR	28	21	19	32	30	28	26	44	41	28	27	23	44	29	43	35	38	46	37	23	39	44	42	51	40

```
TABLE IV A PROGRAM AND THE COMPUTATION OF INCOME TO OWNER OPERAT
       RENTERS,AND LANDOWNERS.

  MARGIN 5 LINE                          EVALUATION OF ALL PERIL CROP INSURANCE
  CRPINS.WKS                               TYPICAL 1/2 SECTION OF 300 ACRES
  R60C16                                     GOAL HALF CROP HALF FALLOW
-----------------------WHEAT------------------------------------------------------------------ OWNER ---------------
     INPUT DATA CALCULATION IN THIS COLUMN       :            FARM OPERATION   $ / AC. NO. TIME TOTAL  OPERATOR  LAND
-------------------------------------------------:-----------------------------------------------------------------------

WHEAT YLD BU/AC    34.44   SPRAY $/AC.      .00:              SPRAY $/SC =        0     .00
       ACREAGE        90   SPRAY NO. X'S      0:              BLADE $/AC =     4.09      5 1840.50 1840.50
         PRICE      2.60   BLADE $/AC      4.09:              DRILL $/AC =     4.17        375.30  375.30
  HARVEST $/AC (   11.57   BLADE NO. X'S      5:              SEED  $/AC =     2.00        180.00  180.00
       %AC, CUT     1.00   DRILL $/AC      4.17:             INSURANCE $/AC.   5.10        459.00  306.00  153.00
       BASE BU.       20   BU.  SEED /AC    .50:            ------------------------------------------------------
       BU/-BASE       16   COST SEED/BU.   4.00:                   FARMING EXPENSES            2855    2702     153
       $/BU OVE      .11   INS. LEVEL 2     .65:            ======================================================
    HAUL $/BU.       .11   INS. $/AC5.10    .00:            HARVEST COSTS PER ACRE             2396    2396     .00
      MILES TO         9   HARVE AC -INS    .00:            ------------------------------
      BASE MI.         9   INC $/BU 2.60    .00:     AC. HARV  $/AC  YLD-BASE  HAUL  TOTAL
      + MI. R1         0   UNPROVE YIELD    .00:     ----------------------------------------------------------------
      + OVER         .01   ACRE INSURED     .00:        90.00  11.57    1.84    3.96  17.37    1563    1563     .00
                                                :                                           :-----------------------
                                                :     WHEAT INCOME    ACRES  YIELD  PRICE  :    4418    4265     153
                                                :     --------------------------------------:
                                                :     WHEAT INCOME       90.00  36.00   2.60    8424    5616    2808
                                                :     INSURANCE INCOME       0     19   2.60       0       0       0
                                                :                                           -----------------------
                                                :                        NET INCOME WHEAT      4006    1351    2655
================ MILO ================================================================MILO============================
      BU./AC      34.44   SPRAY $/AC.      7.50:             FARM OPERATION $ / AC. NO. TIME TOTAL  OPERATOR  LAND
       ACRES      60.00   SPRAY NO. X'S       2:            ---------------------------------------------------------
       PRICE       1.85   BLADE $/AC       4.50:             SPRAYING           7.50   2.00  900.00  900.00
  HARVEST $/AC    11.34   BLADE NO. X'S       2:             BLADING            4.50   2.00  540.00  540.00
     %AC, CUT      1.00   DRILL $/AC       4.94:             DRILLING           4.94   1.00  296.40  296.40
     BASE BU.        31   LB.  SEED /AC       3:             SEED               2.40   1.00  144.00  144.00
     BU/-BASE        11   COST SEED/LB.     .00:             INSURANCE          4.20         252.00  168.00   84.00
   HAUL $/BU.       .11   INS. RATE         .65:                                     ::---------------------------
       MILES          8   INS. $/AC4.20     .00:                                     :: + INS   2132    2048      84
     BASE MI.         0   AC. HARV. INS     .00:     AC. x %   $/AC    HAUL   TOTAL  :: - INS   1880    1880       0
      + OVER        .01   INS $/BU INS     1.85:     -----------------------------------::---------------------------
===============================================:HARVEST     .00  12.55    4.66  17.21              0       0     .00
EVALUATION OF ALL PERIL CROP INSURANCE         ::                                           ------------------------
   TYPICAL 1/2 SECTION OF 300 ACRES            ::     MILO INCOME    ACRES   YIELD   PRICE  :    2132    2048      84
     GOAL HALF CROP HALF FALLOW                ::     --------------------------------------:
     WITH AND WITH OUT INSURANCE               ::               INS.          60      23   1.85    2606    1738     869
          SCOTT COUNTY                         ::               CROP           0      42   1.85       0       0       0
                        FARMING COSTS ARE BASED ::                         ----------------------------------------------
                        ON WC KS. CUSTOM RATES  ::                                            OWNER              LAND
                        TAXES ON LAND ARE $4/AC.::                                         OPERATOR OPERATOR OWNER
                        5 X CALCULATIONS BASED  ::                            ------------------------------------------
                        ON 1/2 SECTION          ::     $ / BU. BUSHELS INCOME  NET INCOME MILO      474     -311     -84
                                                ::-----------------------------NET INCOME WHEAT     4006     1351    2655
                                                                                        ------------------------------
                         OWNER               LAND::
                        OPERATOR  RENTER    OWNER::     1/2 SECTION 300 CULTIVATED ACRE INCOME=    4480     1040    2571
------------------------------------------------::=====================================================================

WHT =36 BU MILO 42 BU/AC    20630     5200    15765::THESE FIGURES:WHT =36 BU MILO 42 BU/AC INSURED   20630     5200   15765
        SAME YIELDS NOT     24185     6678    16950::ARE 5 TIMES  :         SAME YIELDS NOT  INSURED   24185     6678   16950
NO CROP INCOME       NOT   -26240   -28610    -6045:: 1/2 SECTION :NO CROP INCOME      NOT   INSURED  -26240   -28610   -6045
NO CROP INCOME               9255     -435     7995::INCOME LESS 4:NO CROP INCOME              INSURED    9255     -435    7995
NO WHEAT           CROPS     9495    -2175     9213:: 4$/AC LAND    NO WHEAT           CROPS INSURED    9495    -2175    9213
NO MILO            CROPS    17540     5200     7995:: TAX           NO MILO            CROPS INSURED   17540     5200    7995
======================================================================================================================
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Did the Plow Reduce Wind Erosion?

(By Donald Christy)

The blow dirt covered the bones of buffalo with the skulls lying on the leg bones. The stinous processessit vertebra, the bones that stick up from the spine, were still pointing at a natural carcass angle. This suggests a major dirt storm of yester-year.

Buffalo Jones in his book, "Buffalo Jones," wrote that he and Walter Wood's dad were freighting, by wagon, from Garden City to Oakley. On one trip the dirt storm was so bad that they could not continue the trip. They stayed overnight in Scott City where the only inhabitant was a woman who lived in a dug-out. He also wrote of a prairie fire that reached them in three days.

The prairie grasses, buffalo, blue gram- ma and side oats gramma, mature and seed in early summer. That results in a dry, burnable grass in the lightning-affluent thunderstorm season. The result would be numerous winters without cover. During the 1930s a part of some pastures had to be furrowed to stop the blowing.

Herb Coffin, one of the old-timers, told me that his dad told him that the Indians regularly burned the prairie every spring to slow the northward movement of the buffalo.

The accompanying picture of the buffalo, listed as the last of the wild ones, was taken 15 miles north of Scott City in the spring of 1873. The Reeds, early settlers, were the mounted riders in the picture. The buffalo were on land that I have farmed for the last 45 years. The grass in the picture is probably typical of that left by the millions of buffalo that populated the prairies.

The first major recorded Western Kansas drought began in September of 1872 and lasted through the summer of 1875. The Kansas State Board of Agriculture "Climate in Kansas" cites Dr. James Marlin, professor of history at the University of Kansas in the Kansas Historical Reports of 1946. These reports indicate that there were storms as severe as any of those in the 1930s.

Dr. Marlin reports a late April 1890 dust storm in eastern Colorado so severe that it killed 20 percent of the range stock. A late 1895 storm was so severe that 5,000 head, between Larned (Ks.) and Lamar (Colo.), smothered. One Gray County farmer lost 32 out of 46 cattle.

Climate in Kansas reports: "It is interesting to note that the 14 southwestern counties of Kansas, where the dust storms of the 1930s were more severe than in any other part of the state produced an average annual yield of 35+ million bushels of wheat over the 5-year period ending with 1945. This is greater than the average yield for the same period in either Missouri, Illinois, Indiana or Iowa and more than 1/6 of the total for Kansas, though these counties comprise less than a 1/6 of the area of Kansas."

My analysis of Kansas agriculture led to the discovery that the top five gross product agricultural counties of Kansas are Finney, Ford, Gray, Haskell and Scott, with about 100-150 million dollars per year.

As a senator I asked the Agricultural Engineering department of Kansas State university to give me an estimate of the energy efficiency of the grain crops of Kansas, based on the energy used compared to the energy produced, the energy used to manufacture the farm equipment, as well as that used directly to produce, and take the crop to a shipping point. The unit of heat, BTU, was used to compare the energy used to the energy produced.

Example: one gallon of diesel fuel (140,000 BTU) should produce 8 bushels of grain which if burned should produce about (2,800,000 BTU), a 20 BTU output per BTU input for the wheat fallow of this area. This is about three times as energy efficient as the grain production in the corn belt.

These aeolian subsoils were surface soils several times. When they are uncovered by a deep cut they rapidly establish a new soil profile much faster than they lose soil by wind and water erosion. My experience has been that if manure is placed on the soil where deep cuts that have been made for irrigation, plus one or two deep-rooted crops, results in a productive soil.

My observations lead me to believe that the road ditches, the weed and leaf catching fences and the many fields of stubble, are more effective in catching the earth-hugging dirt than the burnt prairie with no traps for the heavy, abrading soil particles. The prompt action by the farm operators is an added sifting dirt trap. I was one of the State Board of Agriculture members who flew to southwest Kansas at the beginning of the dirt storms of the 1950s..The effectiveness of wind erosion control was much better on the Kansas side of the line than in Colorado. Colorado had a wind erosion control law but was hesitant in using it, while the Kansas farmers acted immediately and comparatively effectively.

A Mr Finnegan found by using an airplane that a large part of the dust was organic matter. He also reported that it had a fairly high moisture content. I have felt that this was the reason that the humidity was so low during dust storms.

Cars caught out on the road during the recent storm still had their paint. I heard not one report of points of light on barbed wire fences, or of anyone dragging a chain from their car to prevent stalling, due to static electricity. This was common during the '30s

NEWS CHRONICLE
SCOTT CITY, KANSAS
Wednesday, May 10, 1989

Joe Converth
2208 Hart Avenue
Dodge City, KS 67801

Congressman Pat Roberts
Congressional Field Hearing
Great Bend, Kansas

Dear Congressman Roberts:

The following is my statement prepared for the congressional drought hearing in Great Bend, Kansas, on May 20, 1989.

The drought conditions we are experiencing are quite severe. Even the good rains this week are not going to help the remaining wheat very much as it was nearly too late. As the subsoil was very dry, it will take much more rain to make a decent milo crop.

With a small wheat crop and an unpredictable milo crop, the grain elevators in Ford and Hodgeman Counties will be hard-pressed to make any return on their investment. This condition affects all businesses in the county. We would be helped a lot and might even survive if some form of disaster relief was available.

To address the Crop Insurance situation, it is my opinion the cost would be less over the long run to reinstall the Disaster program. Multi-peril crop insurers are being paid a big commission but are not giving the farmer very good service.

The ASCS offices could handle crop insurance at a minimum fee as they have the farmers' records and the personnel to do the work.

As it stands now, the multi-peril companies do not have the adjustors to do a good job of adjusting. Problems occur such as long delays for claims to be processed and requiring farmers to leave strips of ground because adjustors are not certified or qualified to do the work.

Sincerely,

Joe Converth

Joe Converth
Ford County Wheat Grower

Bart Boyd, Chairman
Ford County Wheat Growers
Wright, Kansas
May 19, 1989

Congressman Pat Roberts
Congressional Field Hearing
Great Bend, Kansas

Dear Congressman Roberts:

The following statement has been prepared on behalf of the Ford County Wheat Growers Association for the congressional drought hearing to be held May 20, 1989 at Great Bend, Kansas.

The current winter wheat crop of western Kansas has sustained permanent and irreversible damage. The recent rains, although beneficial, will not change the status of this crop. The subsoil moisture is still depleted and will require above normal rainfall for successful future crops.

The following are suggestions for needed changes to the Farm Program.

1. Contracts for the 0-92 program should be waivered when drought disaster legislation is implemented.

2. Milo planted on destroyed disastered wheat acreage should not have a planting deadline date.

3. More base flexibility in future farm programs is needed. (See attached summary on crop rotation).

The following are suggestions for needed changes to the Crop Insurance program:

1. Adequate loss coverage.

2. Timely and realistic adjustment procedures.

    A. Any yield adjusted below 5 to 7 bushels per acre should be considered 100% loss.

3. Uniform regulations.

    A. Milo planted on disastered wheat acreage that was destroyed before the headed stage should not be considered crop following crop.

4. Automatic renewal provision of the current crop insurance program should be discontinued.

5. Need separate and timely deadline dates for purchasing crop insurance on corn and milo crop.

Thanks for the opportunity to present a statement at this congressional hearing on behalf of the Ford County Wheat Growers.

Sincerely,

Bart Boyd

Bart Boyd, Chairman
Ford County Wheat Growers
Wright, Kansas

SUMMARY

THE FOLLOWING BENEFITS OF CROP ROTATION WOULD BE REALIZED IF SUBSTITUTION WERE PERMITTED IN PRESENT FARM PROGRAMS ADMINISTERED BY U.S.D.A.

1. NATURAL CONTROL OF WEEDS AND INSECTS

Less reliance on chemicals would reduce the risk of environmental contamination and have a desirable positive effect on the ecological system.

2. REDUCTION OF FERTILIZER

The ability to utilize natural sources of fertilizer would greatly reduce the potential for contamination of our surface and aquifer water supplies by chemical fertilizers.

3. WATER CONSERVATION

In addition to conserving our declining water sources, it would reduce the potential hazard of nitrates and other chemicals being leached into aquifers through intensive irrigation practices.

4. SOIL CONSERVATION

Soil erosion by water and wind would be greatly reduced. Substitution would permit maximum utilization of rotational strip farming on soils that are subject to wind erosion. It would also facilitate and promote more efficient use of irregular shaped terraced fields. Some of the current farm program requirements are in direct conflict with individual soil conservation farm plans.

5. WILDLIFE CONSERVATION

Crop substitution and rotation would result in less reliance on chemicals and intensive cropping practices, therefore, the habitat and environment for wildlife would be enhanced by the cultural practice of crop rotation.

6. COST EFFECTIVE

All of the practices mentioned above would be more cost effective than those mandated by the present farm program. The inability of the farmer to substitute program crops results in higher production costs which further contributes to a depressed farm economy.

Crop substitution would be a major step in accomplishing these goals. The logic and multiple benefits of using crop rotation and substitution would appear to be irrefutable.

SUBMITTED BY: LEON TORLINE
FORD COUNTY WHEAT PRODUCER

Presentation and Information

Provided by

Walter S. Hittle

Farmer & Rancher

Stevens County Kansas

I. Disaster Losses for the High Plains for 1989

A. Dryland Production

1.) Most of the High Plains from Hereford,Texas to Western Nebraska has experienced extreme drought,greenbug infestation ,and winterkill damage to most of its wheat,barley and oats.

2.) Harvestable acres will have very low yields and will be terribly expensive to harvest. Wheat has headed out from 4-8 inches in height. Weed pressure will be tremendous when rains come complicating harvest worse than normal.

3.) Estimated loss from Amarillo to Norton, Kansas will be approximately 80%.

4.) FCIC coverage judging from Southwest Kansas counties is less than 5% of all dryland wheat.

B. Irrigated Production

1.) Estimated loss from Amarillo, Texas to Colby, Kansas 70% loss:Actual yields of wheat left for harvest will 50-65% of normal. 15% of fields are a total loss.

2.) Extreme winterkill and greenbug pressure has devastated the area causing other problems to arise such as diseases.

3.) FCIC coverage judging from Southwest Kansas counties is less than 5% of the total.

C. Pasture Conditions are the worst in 35 years.

II. All Risk Insurance for the High Plains

A. Reasons for historically poor sales

1.) Sales Agents not knowledgeable of unit divisions and all options available.

2.) Bad Reputation of FCIC in being able to cancel out of coverage. Dates to cancel coverage not clear to producer.

3.) Unit divisions not totally explained.

4.) Having to insure all acreage within a county.
Example: Must insure dryland as well as irrigated acreages.

5.) The percent of coverage is not high enough for an irrigated producer to want to participate as it makes coverage to expensive for the dollar spent.

Example: Irrigated Corn Yield 150 bushels
Guarantee 75% X 150 bushels= 113 bushels

If an irrigated corn grower grows the 113 bushel guarantee he has already had more loss than he can stand to afford and will still have the premium to pay.

6.) Producers and lenders are not well informed !!!!!

III. ASCS Implementation of the 1988 Disaster Program

A. Training & Software

1.) Training on this program was sufficient in the state of Kansas.

2.) The software to handle this program is the best that ASCS has had since automation has begun.

B. Reasons for Producers not Signing Up

1.) Failure of ASCS to inform producers well enough.

2.) Producers exceeded gross qualifying income of $2 million. Several producers in the high plains may exceed total gross income due to livestock feeding.

3.) Producers did not understand that nonprogram crops qualified for disaster assistance.

4.) Producers are tired of living in the local ASCS office. Other programs are very confusing and producers are tired of all of the red tape although they are very thankful for the help they have received.

5.) Producers were afraid of the fact that they might have to purchase Multiperil Insurance for future years.

IV. Comparison of 1989 with 1988 if Disaster Program is carried over.

Example: Wheat Disaster 100% Loss versus Normal Crop Yield

Target Price:		Advance Deficiency:	Est. Yield:	Normal Yield:
1988	$4.23	$0.612 per bushel	40 bushels	50 bushels
1989	$4.10	0.20 per bushel		

Wheat Market Price:
1988 $3.20/bushel
1989 $4.10/bushel

1988 Projected Payment:
0-35% Loss: No payments
36-75% Loss: Payments 65% of Target Price
76-100% Loss: Payments 90% of Target Price

0-35% Loss: 35% X 40 bu.= 14 bushel loss no payment $ 0.00
36-75% Loss: 40% X 40 bu.= 16 bu. loss X (65% X $4.23) = $44.00
76-100%Loss: 25% X 40 bu.= 10 bu. loss X (90% X $4.23) = $38.07
Total Payment = $82.07

Returns From a Normal Crop:

50 bushels X $ 3.20 = $160.00 per acre

1989 Projected Payment if Legislation is carried over:

0-35% Loss: 35% X 40 bu. = 14 bu. loss no payment
36-75% Loss: 40% X 40 bu. = 16 bu. loss X (65% X $4.10) = $42.64
75-100% Loss: 25% X 40 bu. = 10 bu. loss X (90% X $4.10) = $36.90
Total Payment = $79.54

Returns From a Normal Crop:

50 bushels X $4.10 = $205.00 per acre

References:

5-PA SCOAP Exhibit 5, Feed Grain, Rice,Cotton, and Wheat Programs Short Reference

1-PAD Disaster Assistance, Short Reference

United States
Department of
Agriculture

Federal Crop
Insurance
Corporation

Field
Service
Office

2601 Anderson Avenue
Manhattan
Kansas
66502

Office of Congressman Dan Glickman
401 North Market Street, Room 134
Wichita, Kansas 67202

May 19, 1989

RE: 1989 Wheat Acres Insured by Federal
Crop Insurance Corporation

Dear Congressman Glickman:

Attached for your information are two listings of the amount of wheat insured by the Federal Crop Insurance Corporation. One listing represents counties in your congressional district and the other all Kansas counties. In your district, 45.3 percent of the wheat acreage is insured. The percent of wheat insured for the state is 41.45 percent.

The wheat base acres are from ASCS records. The maximum permitted acres represent 90 percent of the base acres, or the acreage allowed for ASCS programs.

Since the majority of producers are in the Government's farm program, permitted acres were used in determining the percent of acreage insured.

Please contact me if you have any questions.

Sincerely,

Thomas V. Link
THOMAS V. LINK
Director

Attachments

The Federal Crop Insurance
Corporation is an agency of the
Department of Agriculture

FEDERAL CROP INSURANCE CORPORATION
LISTING OF MAXIMUM PERMITTED ACRES vs ACTUAL INSURED ACRES
FEDERAL AND PRIVATE DELIVERY SYSTEMS
1989 CROP YEAR
[redacted]

KANSAS

	COUNTY NAME	WHEAT BASE ACRES	MAXIMUM PERMITTED ACRES	INSURED ACRES	PERCENT OF PERMITTED INSURED
20-077	HARPER	300,324	270,292	108,998	40.33%
20-095	KINGMAN	230,139	207,125	68,730	33.18%
20-155	RENO	332,479	299,231	64,563	21.58%
20-173	SEDGWICK	266,178	239,560	85,268	35.59%
20-191	SUMNER	509,517	458,565	340,881	74.34%

SUMMARY

	STATE	DISTRICT	DISTRICT SHARE
BASE ACRES	13,291,469	1,638,637	12.33%
MAXIMUM PERMITTED ACRES	11,962,322	1,474,773	12.33%
INSURED ACRES	4,958,952	668,440	13.48%
PERCENT OF PERMITTED INSURED	41.45	45.32	

FEDERAL CROP INSURANCE CORPORATION
LISTING OF MAXIMUM PERMITTED ACRES vs ACTUAL INSURED ACRES
FEDERAL AND PRIVATE DELIVERY SYSTEMS
1989 CROP YEAR
MANHATTAN, KANSAS FIELD SERVICE OFFICE

KANSAS	COUNTY NAME	WHEAT BASE ACRES	MAXIMUM PERMITTED ACRES	INSURED ACRES	PERCENT OF PERMITTED INSURED
20-001	ALLEN	54,064	48,658	12,048	24.76%
20-003	ANDERSON	46,959	42,263	12,596	29.80%
20-005	ATCHISON	29,170	26,253	6,976	26.57%
20-007	BARBER	166,286	149,657	23,911	15.98%
20-009	BARTON	244,504	220,054	56,842	25.83%
20-011	BOURBON	33,559	30,203	4,459	14.76%
20-013	BROWN	56,218	50,596	28,177	55.69%
20-015	BUTLER	99,426	89,483	26,682	29.82%
20-017	CHASE	23,375	21,037	3,190	15.16%
20-019	CHAUTAUQUA	17,609	15,848	4,618	29.14%
20-021	CHEROKEE	93,562	84,206	7,028	8.35%
20-023	CHEYENNE	172,100	154,890	88,729	57.29%
20-025	CLARK	97,745	87,970	8,544	9.71%
20-027	CLAY	123,574	111,217	99,968	89.89%
20-029	CLOUD	167,106	150,395	125,762	83.62%
20-031	COFFEY	52,382	47,144	9,184	19.48%
20-033	COMANCHE	93,613	84,252	23,474	27.86%
20-035	COWLEY	151,032	135,929	25,131	18.49%
20-037	CRAWFORD	54,197	48,777	6,369	13.06%
20-039	DECATUR	145,400	130,860	72,703	55.56%
20-041	DICKINSON	205,770	185,193	62,905	33.97%
20-043	DONIPHAN	26,428	23,785	13,649	57.38%
20-045	DOUGLAS	25,830	23,247	1,888	8.12%
20-047	EDWARDS	129,639	116,675	14,792	12.68%
20-049	ELK	23,381	21,043	4,141	19.68%
20-051	ELLIS	135,638	122,074	42,004	34.41%
20-053	ELLSWORTH	123,497	111,147	61,292	55.14%
20-055	FINNEY	245,804	221,224	85,852	38.81%
20-057	FORD	254,495	229,045	29,543	12.90%
20-059	FRANKLIN	33,935	30,541	5,423	17.76%
20-061	GEARY	28,630	25,767	4,180	16.22%
20-063	GOVE	159,674	143,707	64,413	44.82%
20-065	GRAHAM	130,392	117,353	51,723	44.07%
20-067	GRANT	110,312	99,281	14,511	14.62%
20-069	GRAY	203,937	183,543	26,315	14.34%
20-071	GREELEY	198,488	178,639	46,214	25.87%
20-073	GREENWOOD	23,910	21,519	3,953	18.37%
20-075	HAMILTON	166,874	150,187	37,364	24.88%
20-077	HARPER	300,324	270,292	108,998	40.33%
20-079	HARVEY	148,875	133,987	34,107	25.46%
20-081	HASKELL	147,420	132,678	26,673	20.10%
20-083	HODGEMAN	146,273	131,646	63,295	48.08%
20-085	JACKSON	34,197	30,777	14,040	45.62%
20-087	JEFFERSON	22,382	20,144	7,236	35.92%
20-089	JEWELL	170,967	153,870	99,331	64.56%
20-091	JOHNSON	17,157	15,441	5,849	37.88%
20-093	KEARNEY	157,380	141,642	22,124	15.62%
20-095	KINGMAN	230,139	207,125	68,730	33.18%
20-097	KIOWA	102,858	92,572	11,600	12.53%
20-099	LABETTE	94,555	85,099	14,783	17.37%

FEDERAL CROP INSURANCE CORPORATION
LISTING OF MAXIMUM PERMITTED ACRES vs ACTUAL INSURED ACRES
FEDERAL AND PRIVATE DELIVERY SYSTEMS
1989 CROP YEAR
MANHATTAN, KANSAS FIELD SERVICE OFFICE

KANSAS	COUNTY NAME	WHEAT BASE ACRES	MAXIMUM PERMITTED ACRES	INSURED ACRES	PERCENT OF PERMITTED INSURED
20-101	LANE	154,325	138,892	80,934	58.27%
20-103	LEAVENWORTH	17,566	15,809	3,536	22.37%
20-105	LINCOLN	139,247	125,322	91,626	73.11%
20-107	LINN	34,537	31,083	2,823	9.08%
20-109	LOGAN	176,596	158,936	118,996	74.87%
20-111	LYON	48,473	43,626	5,664	12.98%
20-113	MCPHERSON	262,285	236,056	84,804	35.93%
20-115	MARION	174,378	156,940	53,675	34.20%
20-117	MARSHALL	118,463	106,617	52,626	49.36%
20-119	MEADE	147,348	132,613	13,243	9.99%
20-121	MIAMI	24,007	21,606	4.127	19.10%
20-123	MITCHELL	213,739	192,365	197,060	102.44%
20-125	MONTGOMERY	76,687	69,018	21,534	31.20%
20-127	MORRIS	61,452	55,307	29,314	53.00%
20-129	MORTON	98,309	88,478	27,683	31.29%
20-131	NEMAHA	61,257	55,131	18,861	34.21%
20-133	NEOSHO	64,498	58,048	10,268	17.69%
20-135	NESS	197,878	178,090	100,234	56.28%
20-137	NORTON	141,565	127,408	51,365	40.32%
20-139	OSAGE	39,899	35,909	6,615	18.42%
20-141	OSBORNE	160,762	144,686	89,193	61.65%
20-143	OTTAWA	170,387	153,348	152,767	99.62%
20-145	PAWNEE	180,953	162,858	72,894	44.76%
20-147	PHILLIPS	114,603	103,143	48,313	46.84%
20-149	POTTAWATOMIE	34,078	30,670	7,269	23.70%
20-151	PRATT	195,368	175,831	29,590	16.83%
20-153	RAWLINS	184,017	165.615	130,621	78.87%
20-155	RENO	332.479	299,231	64.563	21.58%
20-157	REPUBLIC	121,121	109,009	84,323	77.35%
20-159	RICE	189,703	170,733	54,213	31.75%
20-161	RILEY	32,563	29,307	7,162	24.44%
20-163	ROOKS	143,071	128.764	58,429	45.38%
20-165	RUSH	167,174	150.457	92,106	61.22%
20-167	RUSSELL	130,506	117,455	67,818	57.74%
20-169	SALINE	178.837	160.953	74.341	46.19%
20-171	SCOTT	173,070	155.763	61,922	39.75%
20-173	SEDGWICK	266,178	239,560	85,268	35.59%
20-175	SEWARD	110,239	99,215	6,841	6.90%
20-177	SHAWNEE	30,113	27,102	6,424	23.70%
20-179	SHERIDAN	144,375	129,937	58,806	45.26%
20-181	SHERMAN	235,024	211,522	151,254	71.51%
20-183	SMITH	149,119	134,207	50,906	37.93%
20-185	STAFFORD	180,003	162,003	29,225	18.04%
20-187	STANTON	148,071	133,264	25,816	19.37%
20-189	STEVENS	115,860	104,274	5,766	5.53%
20-191	SUMNER	509,517	458,565	340,881	74.34%
20-193	THOMAS	252,822	227,540	167,411	73.57%
20-195	TREGO	131,711	118,540	39,941	33.69%
20-197	WABAUNSEE	26,489	23,840	8,424	35.34%
20-199	WALLACE	114,223	102,801	50,699	49.32%

FEDERAL CROP INSURANCE CORPORATION
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FEDERAL AND PRIVATE DELIVERY SYSTEMS
1989 CROP YEAR
MANHATTAN, KANSAS FIELD SERVICE OFFICE

KANSAS	COUNTY NAME	WHEAT BASE ACRES	MAXIMUM PERMITTED ACRES	INSURED ACRES	PERCENT OF PERMITTED INSURED
20-201	WASHINGTON	121,492	109,343	72,650	66.44%
20-203	WICHITA	165,679	149,111	67,123	45.02%
20-205	WILSON	69,339	62,405	14,274	22.87%
20-207	WOODSON	36,185	32,566	12,730	39.09%
20-209	WYANDOTTE	2,787	2,508	682	27.19%

STATE TOTALS

BASE ACRES	13,291,469
MAXIMUM PERMITTED ACRES	11,962,322
INSURED ACRES	4,958,952
PERCENT OF PERMITTED INSURED	41.45

Colorado Association of Wheat Growers
5500 South Quebec Street Suite 111 Englewood, Colorado 80111 303-740-4244

STATEMENT OF JIM PELTON, PRESIDENT
COLORADO ASSOCIATION OF WHEAT GROWERS
BEFORE THE HOUSE SUB-COMMITTEE ON WHEAT, SOYBEANS & FEEDGRAINS
FIELD HEARING IN GREAT BEND, KANSAS
MAY 20, 1989

My name is Jim Pelton, president of the Colorado Association of Wheat Growers which represents more than 1,200 Colorado wheat producers. I am also an active wheat producer from Cheyenne Wells in eastern Colorado.

Thank you for this opportunity to testify before this field hearing being conducted by the Wheat, Soybeans and Feed Grains Sub-Committee of the House Agriculture Committee on the Disaster Assistance Act.

The U.S. Department of Agriculture (USDA) predicted on May 11, that Colorado's winter wheat crop will reach just 67.2 million bushels, down 12 percent from the poor 1988 crop and the smallest figure since the 1978 harvest of 57.3 million bushels. Production has averaged 99.7 million bushels during the 1980's.

The Colorado estimate is based upon 2.1 million acres being harvested with an average yield of 32 bushels per acre. However, this projected yield is not a good indicator of Colorado's overall crop condition since this year's abandonment rate is nearly double the average of the past ten years, when 87 percent of the crop planted has been harvested. The May 11, report estimates that 600,000 acres, or 22 percent of the state's 2.7 million acres planted have already been abandoned. Abandonment could still potentially go higher despite recent moisture.

At present Colorado wheat prices which are averaging nearly $4.00 per bushel, and using historic production figures for the 1980's which reflect a loss of nearly 33 million bushels this year, Colorado wheat producers have already lost approximately $130 million of potential income.

The much smaller than normal crop is the result of a combination of extreme high and low temperatures during the winter, spring drought and wind damage. As a consequence of the extreme and abnormal variability in temperatures, substantial irreversible freeze damage occurred.

Moisture received in the past 7-10 days will be more beneficial to wheat producers north of I-70 and Highway 40. However, it will have little impact on increasing yields south of I-70 and Highway 40 since approximately 75 percent of the acreage in that part of the state has already been abandoned and is the area in which most of the abandonment indicated on the May 11, USDA report has occurred.

As a result, most wheat producers in that area will produce little if any wheat for harvest this year. But it is also generally true that wheat producers throughout the entire state will likely see their yields fall significantly from the norm of the 1980's.

Therefore, timely federal assistance is a necessity for many Colorado wheat farmers. The Colorado Association of Wheat Growers (CAWG) believes that wheat producers in the affected areas deserve to receive federal assistance similar to that offered in the disaster assistance package passed last year by Congress. In that regard, CAWG supports the extension of last year's disaster program to include this year's wheat crop.

However, any disaster assistance legislation passed by Congress should not include a requirement that producers obtain multiperil crop insurance under the Federal Crop Insurance Act for the 1990 crop.

The high cost of Federal Crop Insurance coverage and the unfavorable cost-benefit ratio has deterred many wheat producers from obtaining coverage. The levels of insurance coverage presently offered simply don't provide enough benefit coverage to producers.

In addition, any disaster assistance legislation adopted by Congress should also specifically provide for freeze and wind damage.

For those fortunate Colorado wheat growers producing a crop, prices will likely be in the $4.00 per bushel range this next year. USDA is now projecting the national average wheat price for the 1989-90 marketing year in the $3.80 - $4.20 per bushel range.

Hopefully, federal assistance can be funded by rechanneling income deficiency payments that will not be made because of higher than expected national average prices. Budget projections made with regard to wheat deficiency payments in this year's budget were made on the basis of wheat prices being in the $3.60 - $3.80 per bushel range.

For those unfortunate growers not able to produce a crop, federal disaster assistance may be the only possible alternative.

Again, thank you for this opportunity to testify before this distinguished committee. Are there any questions?

This is the poorest wheat crop for Kansas, since the drought of the thirties. The drought of this spring, which was a continuation of the severe drought of 1988, has left us with very little to no subsoil moisture.

Our nations past Presidents and Agriculture leaders, has done nothing in past years, to help the financial situation of its farmers. So in this process, the money made by our farmers were not sufficient to build up savings to tide one over in depressed cropless years.

Since we have lowered the national loan rate on crops and the market prices has climbed to some extent, but these prices didn't rise because of lower loan rate, but by very dry conditions that prevailed over our agriculture area's in America.

There is now talk of farmers having to repay defficiency payments on wheat. First this is intolerable to farmers, because most farmers never did receive the higher prices on last years short crop, which many farmers had to sell early to pay debts on loans to operate his or her farm.

Now, having lost all or nearly all wheat in some area's of Kansas and in other area's the yields will be considerable lower, making for less dollars the farmers will have to spend in towns or cities in our state.

Now, fuel has risen as well as interest, taxes, and all things the farmer has to buy in his farm operation.

If Congress had of increased the loan rate, instead of lowering it, the cash market price of grains woild of stayed higher. because the loan rate forms a foundation to bolster the cash price _ a proven fact.

The grain trade can do anything it so chooses at anytime on market prices. The severe fluctuations in prices at times does no good for our farmers and consumers as store prices never do go down with crop prices. But they do keep a steady increase in prices.

If we are to keep our nations farmers on the land, something will have to be done to carry the farmers through this depressing times as was done in the thirties. I am old enough to know that no farmers in western area's of wheat belt could have stayed on the land without government help. which the government did provide then or even now if we are to stay.

The problem with our nations economy today was caused by our suppose to be Agriculture experts and economist that brainwashed Congress into believing agricullture was not that important to the survival of our nations economy. Since agriculture is our largest economy, you cannot lower it's prices and let everything else rise in price and expect people to consume the production of one another without alot of borrowed money. This is showing up now on our nations debt structure.

Ralph Smith
Kalvesta, Ks 67856
Phone (913) 848 - 2342

Written Testimony of

Jack Staatz

4 th District Member of the Board of
Kansas Farmers Union

For the

Subcommittee on Wheat, Feedgrains and Soybeans
House Committee on Agriculture

May 20, 1989

Great Bend, Kansas

The Kansas Farmers Union and I wish to thank you for bringing this hearing to the drought stricken state of Kansas.

For the record, my name is Jack Staatz. I farm in Dickinson County which is in the east central part of the state.

Conditions continue to deteriorate through much of the heart lands of the nation. The wheat condition in the number one wheat state continues to decline. The oats crop prospecks diminish every day. The corn crop is suffering. Milo isn't being planted. The alfalfa crop is withering. The native and tame grasses are looking like we've had a killing frost. Two years with lack of moisture along with heat waves in the winter time and freezes in May have set the stage for a disaster of gigantic scale.

Gentlemen, with only 27% of the American farmers having Federal Crop Insurance and it being totally inadequate at its' best, you can start to understand the hugh financial problems that are facing the rural people of Kansas as well as elsewhere in the great plains. It therefore becomes essential that there be an extention of the 1988 Disaster Assistance Act or the passage of some simular legislation that would fully address the problem. Without a disaster program countless farmers and ranchers will be faced with financial ruin. A meaningful disaster program would be a boon to all affected producers and yet not be a burden to the tax payers because it could be paid for from the savings in deficiency payments.

The impact of the drought on the livestock producer is enormous. Many of the pastures are unleased because of no water. Stocking rates are greatly reduced in many others because over grazing due to lack of moisture for normal growth last year. Some help has come down from the USDA but more will be needed in the long run to preserve the cow herds of the drought area.

The lack of Cash flow and the turnover of dollars in the drought area is accented by the filing of Chapter 11 Bankruptcy by Alco-Duckwall Chain of stores which operate in an 11 state area, with headquarters in Abilene, and which is mostly in the drought area. This certainly illustrates what is happening to all business, both large and small in the impacted area. So it becomes apparent that Disaster Assistance Legislation would not only help the farmer but it would become urban enchancement as well.

ROCKY MOUNTAIN FARMERS UNION

OFFICE OF THE PRESIDENT

COLORADO, NEW MEXICO & WYOMING

P.O. BOX 39626 • 4605 PARIS STREET • DENVER, COLO. 80239 • PHONE (303) 371-9090

June 1, 1989

The Honorable Dan Glickman
US House of Represenatives
1212 Longworth HOB
Washington DC 20515-1604

Attention: Greg Frazier

Dear Representative Glickman:

As president of Rocky Mountain Farmers Union, I am very concerned about the drought and freeze that has affected the southeastern and western slopes of Colorado. Rocky Mountain Farmers Union is a general family farm and ranch organization representing about 18,000 farm and ranch families in Colorado, New Mexico, and Wyoming.

We in Rocky Mountain Farmers Union are pleased that the Secretary of Agriculture is concerned about the drought and has announced some programs to help alleviate the effects of the drought. We have urged Governor Romer and Colorado state ASCS officials to make these remedies available to affected farmers and ranchers in Colorado. However, many of the provisions of the Secretary's program will be of only marginal assistance to the farmers of this area. We believe the effects of this drought are deeper and more serious than the Secretary realizes.

The following is a county-by-county estimate of yield loss due to winter kill and drought conditions which occured this spring on Colorado's southeastern and western slopes:

Baca County
- 100 % yield loss of barley
- 80 % yield loss of wheat

Bent County
- 100 % yield loss of barley
- 50 % yield loss of wheat

Cheyenne County
- 100 % yield loss of barley
- 60 % yield loss of wheat

Crowley County
- 100 % yield loss of barley
- 95 % yield loss of wheat

Kiowa County
- 100 % yield loss of barley
- 80 % yield loss of wheat

Otero County
- 50 % yield loss of barley
- 50 % yield loss of wheat

Prowers County
- 100 % yield loss of barley
- 66 % yield loss of wheat

(The above estimates were obtained on May 11 per phone confirmation with the ASCS offices in each county.)

Representative Dan Glickman
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June 1, 1989

In addition to the damage to the wheat and barley in the southeastern counties, we have severe damages to the fruit crops on the western slope of Colorado. Unfortunately, I do not, as yet have figures on the extent of the damage, but from all reports we have received, it will be considerable and will have a very adverse impact economically on the west slope.

Farmers in our area have been under economic stresses from forces beyond their control for several years now. Many have not been able to keep up with the furious economic treadmill they have been on. Some have only been able to survive by loan write-downs and other forms of economic assistance. The recent Farm Credit Act has helped to save them from financial ruin; this drought, however, threatens to negate the beneficial effects of the Farm Credit Act.

Assistance to the farmers in this drought must be far reaching and immediate. The magnitude of the drought calls for more comprehensive assistance than the Secretary's plan provides. We suggest the reauthorization of the Disaster Assistance Act of 1988, the act that was instituted last summer to help the drought-stricken farmers of the Midwest. This measure should be amended to address the particular problems of the farmers of this area (such as the peach producers), but there is no need to reinvent the wheel. The legislation worked last time and will work again to help relieve the pressures of the drought and freeze here in Colorado.

We urge you to take strong and immediate action to aid the farmers and ranchers of this area. As you have heard, the conditions here are genuinely disastrous, and unless assistance is swift and generous, we may lose many of the family farmers and ranchers in Colorado.

I thank you for the concern you have shown by holding hearings in Texas and Kansas and for your patience and understanding in receiving this testimony. All of us here appreciate your efforts. I would be glad to try to answer any questions you might have.

Thank you.

Sincerely,

John Stencel

John Stencel, President
Rocky Mountain Farmers Union

cc: Congressman Ben Nighthorse Campbell

Officers
ED FAIR, *President*
JOHN ENGELLAND, *Vice-President*

Directors
CLYDE RICKER - HOWARD D. HALTOM - STEVE SELLERS
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"There is No Substitute for a Farmers Elevator"

Farmers Co-Operative Union

DON DUMLER - *Manager, Secretary*
A Locally Owned, Tax-paying, Community-building Enterprise
STERLING, KANSAS 67579

Honorable Dan Glickman
U.S Representative
Washington, D.C.

Dear Dan:

The majority of Kansas and all segments of agriculture has and is being devistated by the drought that started late in the spring of 1988 and continues at the present time, even though there has been some moisture this week in our county. All farmers in our area have the same problem, with some much more serious than others and without some assistance from Washington, many of our young farmers may be forced out of business, so we urge immediate action that will assist all of agriculture, as we are getting close to planting time for the fall crops.

The wheat crop in Rice County Kansas is expected to be down 80% from a normal year and with no sub-soil moisture, prospects for a fall crop remains very minimal, all of which are having a definite effect on ag. related business's as well. When the farmer has money, they will spend some of it, but with no prospects at this time, they are holding back and our Company is suffering, as are the small rural communities and we could use some assistance as well.

As a Farmer Cooperative that serves in excess of 2,000 farmers and landowners in Rice County Kansas, we are feeling the impact of the drought as well. We have been forced to reduce employee numbers, cut hours and are considering cutting additional services if we cannot see relief shortly. Total sales are down over 25% the first 4 months of the year and grain storage income is down 70% and with little or no prospects in sight for 1989, it will become much worse.

A couple of ways you might help our business, would be to take the message back to Washington and visit with USDA and have them leave any grain that CCC has stored with us in our facilities and remove our name from the Grain Catalogue. This way, we would have a little guaranteed income until things return back to normal, which we believe will be fall of 1990 at the earliest. Since we have reduced employee numbers by 20% and are considering cutting hours, maybe a word with the Department of Human Resources to help share some of the burden, should we reduce the income of the rest of our employee's. They have house and vehicle payments to make, as well as trying to raise families and they need the extra hours of work that they are accustomed to, in order to just get by.

Thank you for your time in reading our requests and do take the word back to Washington for us.

Sincerely
Farmers Cooperative Union

Ronald D. Stice

Ronald D. Stice Operations Manager
512 A Street
Bushton, Kansas 67427

May 20, 1989

Dear Chairman Glickman and members of the committee,

My name is John Sullivan. I am a diary farmer from Superior, Nebraska. My brother Joe and I operate a dairy farm with 400 to 425 head of holstein. About 170 are milking and the balance are dry cows and replacements. We farm approximately 1,850 acres to grow the needed pasture, alfalfa, corn, milo, oats and silage. Our only cash crop is wheat, which is also used for winter pasture. I am the Nuckolls County Farmers Union vice-president and a director of Mid America Dairymen and represent dairyman who sell to Mid America Dairymen from five Kansas and four Nebraska counties.

I believe the drought related problems I face are typical of the problems facing those I represent in Kansas and Nebraska. The drought of 1988 caused us to produce only about half the normal needed feed. Consequently, we have been purchasing alfalfa since the middle of January. Normally, alfalfa hay would not cost over $40 per ton. We have had to pay $80 per ton this year. Many dairymen have paid up to $130 per ton. At the present time, I have about 10 days supply of alfalfa.

The 1989 crop does not look good. Checking fields today I find that in some fields, there is no growth. In others, the hay is four inches tall and not growing. I do have a 21 acre field that I could pump water on, but it will not feed my milking herd more than 10 days. I planted some rye last fall for pasture for my dry cows, but it has died. I planted 70 acres of oats this spring hoping to have it for roughage when I run out of silage. Most of it has died. There is no growth or very little growth to our pastures, so the replacement herd is still being fed silage which I will be out of in two to three weeks.

I am 53 years old and farmed all my life. I have never before planted corn in dust as I did this year. We did receive about an inch of rain May 3 and I am hoping it will bring up the corn. I only have one month supply of corn left from the 1988 crop. Then I will have to buy grain.

This years wheat crop is nonexistent for the most part. Some fields have died from a lack of moisture. I do have multi-peril crop insurance on wheat and milo which will help pay the farming expenses for those crops. I needed it the worst for alfalfa but multi-peril crop insurance is not available for alfalfa. New fields that were planted last fall have only half a stand. The balance died from lack of moisture.

I do not know at this time if I or the dairy producers that I represent can survive. We need rain desperately. The government emergency haying and grazing of ACR acres is of little or no relief. Without rain, nothing can grow on ACR acres. With the present low price for milk, I am afraid many men will be forced to quit producing natures most perfect food.

In my opinion, it would be most helpful if the members of this subcommittee would support the extension of the 1988 Drought Assistance Act so that additional assistance could be made available this year. While I appreciate the action Secretary Yeutter has taken, much more must be done to prevent absolute devastation in our drought stricken areas.

Respectfully,

John Sullivan

DEPARTMENT OF AGRICULTURE
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20250

Honorable Dan Glickman
Chairman, Subcommittee on Wheat,
  Soybeans, and Feed Grains
House of Representatives
Washington, D.C. 20515

Dear Dan:

Thank you for your letter concerning your bill to provide disaster payments and additional crop insurance coverage for producers affected by this year's drought. As I understand it, the bill would provide for disaster payments on 1989-crop wheat, feed grains, soybeans and certain nonprogram crops. It also would reopen the 1989 enrollment for Federal Crop Insurance.

I believe that enactment of drought relief legislation would be premature at this time. Further, I could not recommend to the President that he sign a disaster assistance bill unless it is:

- Budget-neutral and would not lead to a sequestration under the Gramm-Rudman-Hollings provision;

- Applicable only to 1989 crops affected by drought;

- Accompanied by an agreement between the Congress and the Administration that Federal Crop Insurance will be the sole vehicle for crop disaster assistance after 1989. Future crop insurance participation should be required as a condition of eligibility for producers receiving disaster payments for 1989 crops. In turn, the Federal Crop Insurance program must be reformed so that in the future it will provide disaster protection affordable both to farmers and to taxpayers.

I realize that recent rains will not be of much help to winter wheat producers in Kansas and elsewhere. But they will help rangelands and producers of spring-planted crops. The Midwest has had widespread rainfall over the past few days, and forecasts for the immediate future are encouraging. Therefore, I do not believe it would be appropriate to put in place a program that, hopefully, will be unnecessary. Each time the Congress does so, it deals another blow to crop insurance.

The latter is also a concern with respect to legislation that would help winter wheat producers. Crop insurance was available this year throughout the winter wheat belt at rates that bear a considerable taxpayer subsidy. Should the taxpayer now bear still another burden by providing relief to those who chose not to purchase insurance? If ad hoc drought or other disaster relief programs are legislated each year we will never be able to develop viable insurance programs. Participation will decline, and the taxpayer will have to bear that additional cost as well.

That is also why we should not reopen the 1989-crop insurance program. Doing so could add millions of dollars in FCIC losses, and it would essentially convert crop insurance into a disaster payment program. If one can buy insurance retroactively, it is a misnomer to call it "insurance".

Beyond the reduced incentive to participate in the Federal Crop Insurance Program and higher indemnity exposure, the likely cost of the bill's disaster payment provisions is of concern. Most of the outlays for disaster payments under the bill would occur in FY 1990. Meeting the Gramm-Rudman-Hollings deficit target will be difficult under any circumstances, and any new commitments must be evaluated against competing national priorities.

The Department will re-estimate Commodity Credit Corporation (CCC) outlays for price support and related operations for the Mid-Session Review in June or July. Those estimates should capture any changes in program costs for winter wheat. However, we could have offsetting increases in other commodity programs; that is impossible to determine at this time. For the 1989 crop year as a whole, there may be no net reduction in CCC outlays at all. The range of $250 to $350 million mentioned in your letter is our preliminary estimate for winter wheat disaster payments only. We do not yet have updated projections of total 1989 wheat program costs which would enable us to gauge the changes in outlay estimates stemming from the reduced winter wheat crop, nor do we have estimates for other crops.

My judgment, Dan, is that existing legal authority is adequate to help livestock producers in drought-stressed areas. We'll continue to do what we can to facilitate feed supplies and thereby minimize herd liquidations. That situation seems now to be improving. To me it is the most critical element of this year's drought because cow herds are not easily replaced and crop insurance was inapplicable. The case for taxpayer relief for grain farmers, is not persuasive because of the availability of insurance.

Sincerely,

Clayton

Clayton Yeutter
Secretary